Dayton Hudson Corporation Annual Report -- 1978
America's Corporate Foundation; 1978; ProQuest Historical Annual Reports
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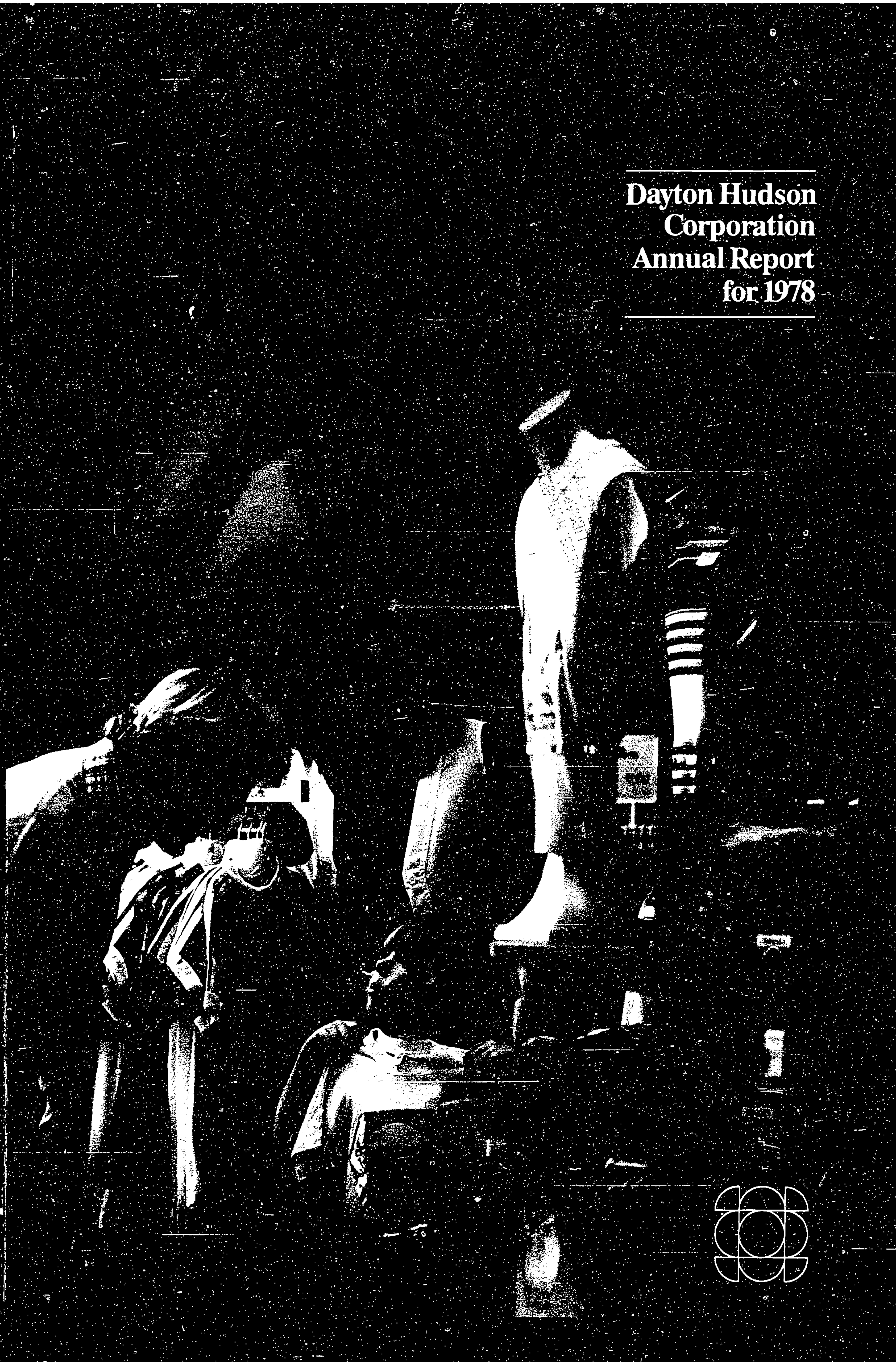
Dayton Hudson Corporation Annual Report for 1978



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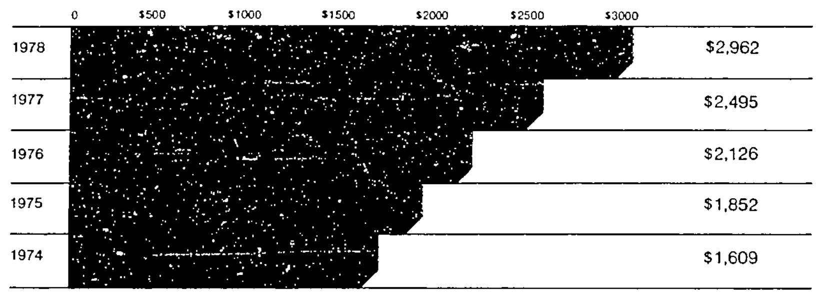
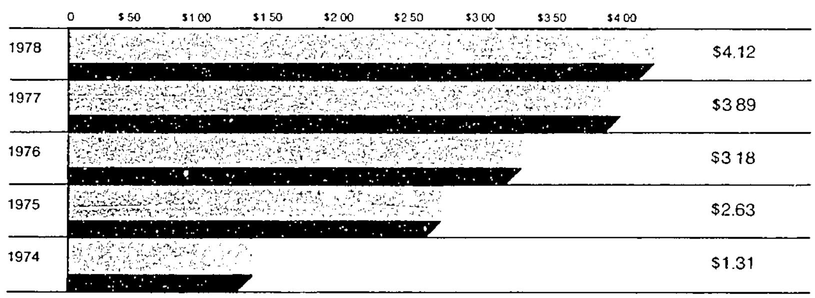
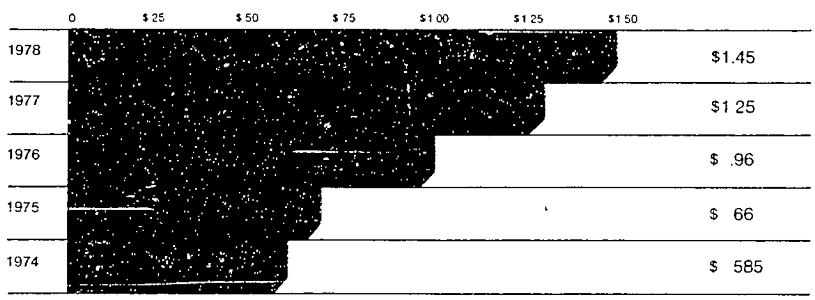
REVENUES (Millions)



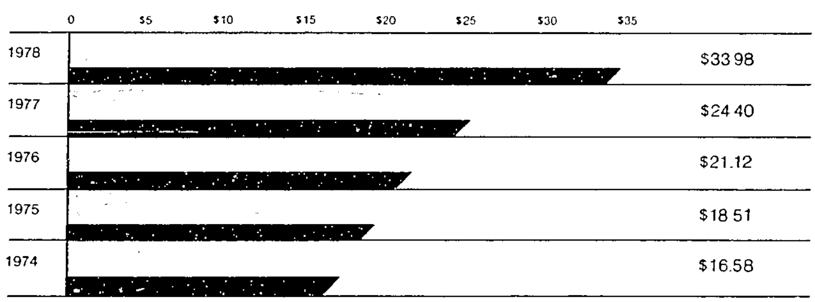
NET EARNINGS PER SHARE



CASH DIVIDEND PER SHARE



SHAREHOLDERS' INVESTMENT PER SHARE



Contents

Dayton Hudson Corporation

Dayton Hudson Corporation operates its Retail business nationally through department stores, low-margin stores and specialty stores. In addition, it operates a chain of softlines stores through its Mervyn's division, which was acquired through a merger in May 1978. The Corporation has announced its decision to discontinue its Real Estate operations. Accordingly, the bulk of its Real Estate assets has been sold or is in the process of being sold. For a description of Dayton Hudson Retail operating companies and their locations, see Pages 38-40

Annual Meeting

The Annual Meeting of Shareholders is scheduled for 10 a.m. Wednesday, May 30, 1979, in the IDS Conference Theatre, on the concourse level of the IDS Center, 80 South Eighth Street, Minneapolis, Minnesota.

Corporate Offices

777 Nicollet Mall
Minneapolis, Minnesota 55402
Telephone: (612) 370-6948

Cover: *Boyswear at new Mervyn's store in Redwood City, California*

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Results From:	1977 (A) 52 Weeks Ended January 28, 1978	Percent Increase
Continuing Operations		
Revenues	$2,494.7	19%
Earnings Before Unusual Expenses and Income Taxes	$ 187.2	17%
Unusual Expenses	—	
Income Taxes	$ 95.5	
Net Earnings	$ 91.7	6%
Net Earnings Per Share	$ 3.89	6%
Cash Dividend Per Share	$ 1.25	16%
Discontinued Real Estate Operations		
Net Earnings Per Share		
Operations	$ .27	
Sale of Shopping Centers	—	
	$ .27	
At Year End:		
Shares Outstanding	23,546,117	
Retail Square Feet	21,625,000	
Number of Stores	516	

(A) Restated to reflect the discontinuance of the Real Estate line of business, the merger with Mervyn's and the inclusion of capital leases.

(B) Exclusive of the effect on net income of the unusual expenses noted above, net earnings per share would have been $4.64 (See Note A to Financial Statements).

All dollars in millions, except per share amounts.

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To Our Shareholders:

The year 1978 was one of the most significant and eventful in the history of Dayton Hudson Corporation. The year is perhaps best characterized by two major accomplishments. First, we achieved record levels in sales, earnings and dividends for the fourth consecutive year.

- Annual revenues increased 19% to $2,961,884,000.
- Earnings from continuing operations—our Retail business—rose to $4.12 per share versus $3.89 in 1977. Before unusual expenses, Retail earnings amounted to $4.64 per share—an increase of 19% over last year.
- Consolidated earnings per share, which include $7.09 from discontinued Real Estate operations, were $11.21.
- The total dividend paid in 1978 increased to $1.45 per common share, up 16% from the $1.25 paid in 1977. The quarterly dividend rose to 40 cents per share in the fourth quarter.

Second, we completed a major strategic plan involving several key transactions and decisions which strengthens our commitment to retailing and which brings us closer to our goal of being recognized broadly as the nation's premier retailer.

- We completed the merger with Mervyn's, bringing to our Retail operations an extremely successful softlines chain of 51 stores in California, Nevada, Arizona and New Mexico. As the largest single expansion ever undertaken by Dayton Hudson, the merger adds significantly to our balance—both strategically and geographically.
- The sale of our nine regional shopping centers to The Equitable Life Assurance Society of the United States was completed in May. The sale, involving the major portion of the Corporation's Real Estate assets, was the first step in the discontinuance of our Real Estate business.
- We reached the decision to sell Team Electronics, our home electronics company, and to discontinue the operations of our Lipmans department stores. Management determined that the business strategies of these operating companies were not compatible with the focus of the Corporation's aggressive Retail growth plans.
- We announced our plans to invest $1.3 billion in retail expansion over the next five years. Nearly 75% of the planned investment will go to the Corporation's three fastest growing companies: Target, Mervyn's and B. Dalton Bookseller.

These actions strengthen our strategic commitment to our basic business, retailing, and will enable us to serve effectively our diverse and expanding customer base with a wide range of desirable shopping alternatives. We believe that together they place us at the forefront of the retail industry as we prepare to enter the 1980s, a decade which holds great promise for retailing and for Dayton Hudson.

Fourth Quarter

Our strongest Christmas season ever resulted in a record fourth quarter for Dayton Hudson Corporation. Revenues for the quarter rose 23% over last year. Earnings from continuing operations were $2.56 per share, up 26% over $2.04 in 1977. Discontinued Real Estate operations provided earnings of 51 cents per share, including 49 cents per share from an additional gain on the sale of the nine regional shopping centers.

Retail Results

Retail revenues were $2,961,884,000 in 1978, an increase of 19% over last year. Retail earnings rose to $4.12 per share, compared with $3.89 in 1977. Excluding the effect of three unusual expenses, Retail earnings amounted to $4.64 per share, an increase of 19%. The unusual expenses include:

- Fees relating to the Mervyn's merger of 12 cents per share.
- A provision for the planned closing and demolition of the Hudson's store in downtown Detroit of 32 cents per share.
- A provision for loss on the discontinuance of our Lipmans department stores and the planned sale of Team Electronics of 8 cents per share.

All segments of our Retail operations contributed to our profitability in 1978. Department stores again provided the Corporation with its largest single source of revenues and operating profit—39% and 46%, respectively. The low-margin group recorded the largest gain in operating profit, a 31% increase over the previous year.

Among individual companies, Hudson's ranked first in total operating profit and second in total revenues. The Detroit-based department store company posted an 18% gain in earnings, while revenues were up 12% over the previous year.

Target's 23% increase in annual revenues strengthened its position as the Corporation's leading revenue producer. In terms of operating profit, which was up 32% for the year, Target ranks second among all of our operating companies.

Mervyn's continued to display the strong pattern of growth which has made it one of the best performing companies in the retail industry. In its first year as a Dayton Hudson subsidiary, Mervyn's led all operating companies in revenue growth with a 30% increase. Operating profit exceeded expectations, increasing 19% over 1977. Before the conversion of Mervyn's to the last-in, first-out method of inventory accounting, operating profit increased 31%.

Dayton's showed improvement in both sales and earnings despite the major remodeling which took place throughout much of the year in two of the company's stores in Minneapolis and St. Paul.

Lechmere, our Boston-based hardlines retailer, continued to expand its market share and reported a 21% increase in operating profit on a 21% rise in revenues.

Our western department stores recorded a slight decline in operating profit for the year. Revenues increased 14%.

Dayton Hudson Jewelers recorded the sharpest increase in operating profit, 38%, on a revenue increase of 12%.

B. Dalton Bookseller had a 26% increase in annual revenues, while operating profit was up 12%.

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Real Estate

Net earnings from Real Estate operations were $7.09 per share. The earnings figure includes a capital gain of $6.88 from the sale of the nine shopping centers. Real Estate earnings in 1977 were 27 cents per share.

As reflected in our financial statements and elsewhere in this report, the decision has been made to discontinue our Real Estate business. Negotiations are continuing for the sale of all the Corporation's remaining Real Estate investment assets, including three wholly owned centers, our interest in four operating joint-venture shopping centers and other properties that are in various stages of development.

Financial Position

We continued to improve our strong financial position in 1978. As the year progressed, our conservative financial policies clearly proved their effectiveness as a counterbalance to our aggressive growth programs. At year-end, the debt ratio of our Retail business, including capital leases and the present value of all operating leases, was 32% of total capitalization, compared with 38% at the end of 1977.

Capital Investment and Expansion

Our investment in Retail expansion increased significantly in 1978. The total investment, including capital expenditures and the capitalized value of new lease obligations, was $192 million, compared with $130 million in 1977.

Retail space increased to 24.2 million square feet during the year. Store openings included five department stores, nine low-margin stores, nine Mervyn's stores and 62 specialty stores.

Retail capital investment in 1979 will total approximately $235 million. Scheduled openings include one department store, 10 Mervyn's stores, 13 low-margin stores and 79 specialty stores for a total of approximately 2.5 million square feet of additional Retail space, an increase of 10%.

Management and Board Changes

As part of our continuing efforts to strengthen our management team, we completed a reorganization plan in November which further balances the administrative load among President and Chief Operating Officer Stephen L. Pistner, Vice Chairman and Chief Administrative Officer Richard L. Schall, and myself.

The reorganization brings all Retail operations under the direction of Mr. Pistner. C. George Scala, Senior Vice President and Group Officer, is responsible for the operations of John A. Brown department stores, B. Dalton Bookseller and Dayton Hudson Jewelers. Mr. Scala, who reports to Mr. Pistner, was with Hudson's from 1949 to 1974, most recently as Senior Vice President-General Merchandise Manager.

The Board of Directors added two new members during the past year, increasing the size of the Board to 15. Donald J. Hall, President and Chief Executive Officer of Hallmark Cards, was elected in September. Mr. Hall is the ninth non-management director. Mervin G. Morris, Chairman and Chief Executive Officer of Mervyn's, was elected to the Board in January.

The Future

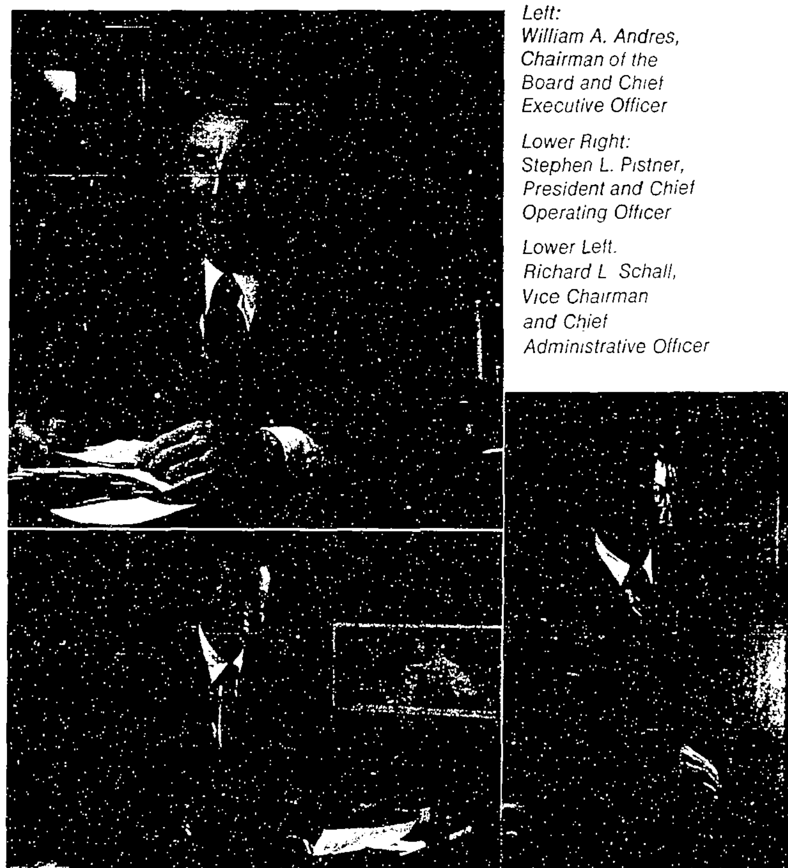
The economic outlook for 1979 indicates the probability of a mild recession in the second half of the year. Accordingly, we are ready to implement a set of contingency plans in the event that retail sales show any significant softening. These plans have been developed by each operating company and are based upon maintaining flexibility in both inventories and expenses, two factors which will receive very close attention throughout the entire year.

In spite of the possible downturn in the economy, we remain optimistic about the prospects for Dayton Hudson Corporation in 1979. First quarter sales continue to show good improvement over last year. We believe that our ability to respond quickly to the consumer, our strategic and geographic balance and our strong management will enable us to perform well during the coming year.

William A. Andres

April 16, 1979

William A. Andres
Chairman of the Board
and Chief Executive Officer



Left:
William A. Andres, Chairman of the Board and Chief Executive Officer

Lower Right:
Stephen L. Pistner, President and Chief Operating Officer

Lower Left:
Richard L. Schall, Vice Chairman and Chief Administrative Officer

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Commitment to Retailing

Serving the demanding and changing needs of an expanding consumer base is the essence of our Retail business. On a day-to-day basis, we accomplish this by anticipating change, by responding to it quickly and forcefully and by capitalizing on trends.

While this short-term response to change is critical, longer-range decisions form the basis for keeping each of our operating companies strategically positioned to respond to the customer.

Within each of our companies, we employ a planning process which includes a thorough annual review of each company's strategic direction and long-range plans.

The same process is used at the corporate level to insure that we are making the strategic decisions today that will keep us well positioned to respond profitably to retailing opportunities in the future.

Decisions generated by this planning process came to fruition in 1978 with the discontinuance of our Real Estate business, the merger with Mervyn's, and the decision to discontinue the operation of Lipmans and to sell Team Electronics.

The result has been the strategic refinement of Dayton Hudson's business.

Retail results for 1978 compared with the *historical* outcome of 1974 demonstrate the extent to which our business has evolved over the past five years—change that has resulted from the strategic planning process that has been an integral part of our management process over the same time period.

STRATEGIC BALANCE

	Revenues		Operating Profit	
	1978	1974	1978	1974
Department Stores	39%	56%	46%	72%
Low-Margin Stores	36	36	28	24
Specialty Stores	9	8	8	4
Mervyn's	16	0	18	0
	100%	100%	100%	100%

From another perspective, our business now serves a larger and far more diverse customer constituency than in 1974. Today, through a variety of retail formats, Dayton Hudson is broad in scope. Yet it is focused in approach through the commitment of each company to serve its own customers, its own markets.

Each of our Retail companies operates within separate and distinct business strategies which, through merchandise assortments, market areas and fashion and price levels, represent a unique approach to the consumer.

In 1978 our diversity and balance was enhanced—both strategically and geographically—by the merger with Mervyn's. The addition of this outstanding softlines chain gives us another unique and desirable retail format.

The major strategic transactions and decisions which took place in 1978 all point to our commitment to the Retail business. There is perhaps no stronger statement of this commitment, however, than our Retail expansion plans announced during the past year.

During the five-year period 1979-1983, we plan to invest $1.3 billion in Retail expansion. Of this amount, more than $1.1 billion will be in capital expenditures and nearly $200 million in new lease obligations. In addition, $200 million in working capital will be used to support new stores. The planned expansion will give Dayton Hudson more than 1,100 stores by 1983.

The current expansion plan represents a logical extension over last year's plan and takes into consideration one very important new factor, the addition of Mervyn's to our Retail operations.

Nearly 75% of the total planned investment will go to our three fastest growing companies: Target, Mervyn's and B. Dalton Bookseller. Over the five-year period, 45% of the total investment will go to low-margin expansion; 20% to department stores; 15% to specialty stores; and 20% to Mervyn's.

As has been the case throughout our history as a public corporation, the focus of our efforts, and the reason for our strategic as well as operating plans, is to provide our shareholders with an optimum return on their investment over time. We view our long-term profits as a reward for effectively serving our customers and the communities in which we operate.

While serving customer needs is the essence of our business, we continue to place a high priority on serving our communities as well. One expression of this service is our policy of contributing an amount equal to 5% of our taxable income from operations toward projects which improve the quality of life in the communities of which we are a part.

For the 1978 program, funds expended by the Corporation, operating companies and the Dayton Hudson Foundation totaled $7.9 million. A copy of the report on contributions in 1978 can be obtained by writing to the Senior Vice President, Environmental Development.

Dayton's Oval Room: Designer fashions for women.

Sportswear boutique a
Hudson's Sterling Heights stor

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Department Stores

Providing the Cornerstone

The department store group continued its position as Dayton Hudson's leading source of revenue and operating profit. Annual revenues increased 11% to $1,172,325,000. Operating profit increased by the same percentage to $115,307,000.

Hudson's once again set the pace for the group in sales and earnings growth. Annual revenues were up 12% over the previous year, while operating profit rose 18%. Dayton's revenues increased 9%, approximately the same amount as last year's gain. Operating profit was up 4%, despite major remodeling which took place in two of the company's stores during the year.

Annual revenues from the western stores—Diamonds, Lipmans and John A. Brown—increased 14%. Operating profit declined from last year's level. While Lipmans and John A. Brown both recorded operating profit gains, the group's total earnings were adversely affected by a 19% decline in Diamonds' operating profit. The decline was primarily due to a significant rise in operating expense which accompanied a 29% increase in retail space in 1978.

John A. Brown led the western stores in earnings growth in 1978 with an 11% gain in operating profit. Annual revenues were up 13%. John A. Brown's strong market position has enabled the company to retain its traditional emphasis on value while building its fashion business in the upper price lines. As a result, it has been able to serve effectively the needs of a young, well-educated customer with an above-average level of disposable income.

Five new department stores opened in 1978, increasing the group's total to 51 stores in nine states. Hudson's opened its ninth store in the Detroit area in February 1978. The new store, a 206,000-square-foot unit in Sterling Heights, brings the company's total stores to 15. At the same time, Diamonds added a second store in Nevada with the opening of a 125,000-square-foot unit in West Las Vegas. In January 1979, Diamonds opened a 125,000-square-foot store in Paradise Valley, Arizona. The new store is the company's fifth in the Phoenix area and ninth overall.

Revenues	1978	1977
Hudson's	$ 644,088,000	$ 575,053,000
Dayton's	334,867,000	308,620,000
Diamonds	98,270,000	82,393,000
Lipmans	49,387,000	46,744,000
John A. Brown	45,713,000	40,495,000
Total	$1,172,325,000	$1,053,305,000

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Department Stores (continued)

Dayton's continued its expansion into regional locations in August, opening 100,000-square-foot stores in Grand Forks, North Dakota and Sioux Falls, South Dakota. The Sioux Falls store is Dayton's first in South Dakota. The new regional stores bring to five the number outside the Minneapolis-St. Paul area, and increase the company's overall total to 15.

Early in the first quarter of 1978, Dayton's re-opened a home store in a new freestanding location near Southdale Shopping Center in suburban Minneapolis. The 83,000-square-foot multi-level unit, the largest of Dayton's three home stores, features over 250 room vignettes showing full assortments of all styles of furniture and home accessories, including carpeting, drapes and appliances. The store replaced a smaller facility which was located adjacent to Dayton's department store in the Southdale Center.

Hudson's: Introducing fashion trends through quality presentations.

Gourmet housewares at Dayton's.

One new department store is scheduled to open in 1979. In July, Hudson's will open its sixteenth store, a 103,000-square-foot unit in West Lansing, Michigan.

In July 1978, the Board of Directors authorized the closing and demolition of Hudson's downtown Detroit store in 1982. In 1978, the downtown store accounted for approximately 9% of Hudson's total annual revenues. With total retail space of approximately 1.5 million square feet, the store is too large to operate economically at present and anticipated sales levels.

The Board of Directors has also approved the construction of a new 320,000-square-foot Hudson's store in downtown Detroit. The approval is contingent upon completion of a downtown shopping center project to include at least two other major department stores, as well as additional tenant areas, public parking and residential housing.

At the beginning of fiscal 1979, the Corporation announced that it was discontinuing the operations of its Lipmans department stores through a sale and an exchange of stores and other assets among Lipmans, Mervyn's and Frederick & Nelson, a Seattle-based division of Marshall Field & Company. Under the arrangement, Mervyn's will enter the Oregon market by remodeling and re-opening three stores formerly occupied by Lipmans and Frederick & Nelson.

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Low-Margin Stores

Low-margin stores became the second Dayton Hudson Retail group to top the $1 billion mark in annual revenues, as revenues increased 23% to $1,055,048,000 in 1978. Operating profit increased even more sharply, rising 31% to $71,715,000.

Target proved once again that it has successfully met the challenge of combining rapid growth with profitability. Earnings outpaced sales in 1978 as operating profit increased 32% over the previous year. The company widened its lead as the Corporation's leading revenue producer with a 23% increase.

Serving family shoppers at Target's newest Minnesota store in East St. Paul.

Revenues Top $1 Billion

A key factor in Target's consistent growth in revenues and earnings is its ability to recognize and react to a constantly changing customer base. As a result, Target has become well-positioned to serve the everyday shopping needs of not only the young family, but consumers of all ages and demographic patterns who today increasingly shop for value as well as quality.

Lechmere's revenues and operating profit each increased 21% over 1977. The company, based in Boston, continues to refine its particular mode of retailing. Its business is built around a group of core departments—television, major appliances and audio components—which feature the market area's largest selections of the most popular models and brands. These core areas are augmented by additional hardlines merchandise categories such as sporting goods, cameras, jewelry and housewares.

Revenues	1978	1977
Target	$ 898,671,000	$729,027,000
Lechmere	156,377,000	129,754,000
Total	$1,055,048,000	$858,781,000

At fiscal year-end, Target operated a total of 67 stores in 10 states within the central part of the country. Eight new Target stores were opened in 1978. Six of the new units are located in existing markets—the second in Tulsa, third in Des Moines, sixth in Dallas, seventh in both Houston and Denver, and twelfth in Minneapolis-St. Paul.

The success of two 100,000-square-foot stores which opened in Fargo and Grand Forks, North Dakota last summer is an encouraging start to Target's expansion into smaller communities

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High-volume hardlines at Target.

within well-established marketing areas. The Grand Forks store is the company's first regional shopping mall anchor, opening a new set of site selection alternatives as expansion into similar markets continues.

Target will step up its expansion program in 1979, opening 13 additional stores, including its first three in Ft. Worth. The company will continue its move into the Dakotas, with new stores scheduled for Bismarck, North Dakota, and Sioux Falls, South Dakota. Other new units will be balanced between new and existing markets.

In October, Lechmere opened its sixth store, a 110,000-square-foot unit in Framingham, Massachusetts. The store is the second to utilize the company's new prototype design which emphasizes maximum selling space and flexibility to accommodate rapidly changing merchandise trends.

Lechmere recently completed construction of a new distribution center in Woburn, Massachusetts, near Boston. The 210,000-square-foot facility is a key element in Lechmere's plans and will help to streamline the company's inventory and distribution procedures.

Specialty Stores

New Stores and New Markets

Revenues from specialty store operations increased 19% to $255,006,000 in 1978. Operating profit increased 6%.

B. Dalton Bookseller led the specialty store group in revenue growth with a 26% increase over last year. Operating profit increased 12%. The earnings gain was achieved in spite of higher operating expenses resulting from increased wage rates, as well as higher start-up costs in connection with an expanded store opening program.

Revenues from Dayton Hudson Jewelers were up 12%, while operating profit showed even greater improvement, increasing 38%, the sharpest earnings gain in the Corporation.

Although revenues from Team Electronics increased slightly over last year's level, the company recorded an operating loss in 1978. Management is continuing its efforts to find a buyer for the home electronics subsidiary.

Broad assortments, personalized service...

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New stores added significantly to B. Dalton's sales growth in 1978. The company opened 60 new stores, including its first in Arkansas, Maine, Montana and Wyoming. At year-end, B. Dalton operated 357 stores in 43 states.

One of B. Dalton's key strengths is its well-defined store prototypes which have been designed to serve virtually

Revenues	1978	1977
B. Dalton Bookseller	$174,397,000	$137,965,000
Dayton Hudson Jewelers	42,017,000	37,645,000
Team	38,592,000	37,973,000
Total	$255,006,000	$213,583,000

any market size. The primary store prototype, a 3,500-square-foot unit carrying approximately 30,000 titles, serves areas with a minimum population of 150,000. For middle-size markets, B. Dalton offers a secondary store of approximately 2,200 square feet. A tertiary prototype with 1,500 square feet and approximately 10,000 titles serves the company's smallest market areas. While the majority of the stores are located in shopping malls, an increasing number are opening in central business districts and suburban free-standing locations.

Of the new stores opened in 1978, 28 were primary prototypes, 10 were secondary, and 17 were tertiary. In addition, B. Dalton opened five central business district stores, including the company's two largest units: a 20,000-square-foot store in downtown Chicago and a 25,000-square-foot store in Midtown Manhattan.

B. Dalton will accelerate its expansion program in 1979, with approximately 75 stores scheduled to open throughout the country. The company also will open its first store outside the continental United States, a 3,000-square-foot unit in San Juan, Puerto Rico.

Dayton Hudson Jewelers added two new stores during 1978, increasing its total to 45. Shreve's opened its seventh California store, while Caldwell's added a second in Delaware, bringing its total stores to seven. Four new jewelry stores are scheduled to open in 1979.

New Shreve's jewelery store in Cupertino, California.

B. Dalton on Nicollet Mall — a central business district store in Minneapolis.

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Mervyn's

In May, shareholders approved the merger of Dayton Hudson Corporation and Mervyn's, a California-based softlines retailer. The transaction was accounted for as a pooling of interests involving the exchange of approximately 7.6 million shares of Dayton Hudson common stock for all outstanding shares of Mervyn's.

In its first year as a Dayton Hudson operating company, Mervyn's led the Corporation in revenue growth. Revenues were up 30% to $479,505,000, making it the Corporation's third largest source of revenue. The company also finished the year ahead of plan as the third largest contributor of operating profit, with a 19% increase over the previous year.

Women's apparel at Mervyn's.

Mervyn's distribution center in Hayward, California.

Adding to Strategic and Geographic Balance

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At the end of the year, Mervyn's changed to the last-in, first-out (LIFO) method of inventory accounting, resulting in a charge to earnings. Before this change, Mervyn's operating profit improved 31% over 1977.

Among the nine stores Mervyn's opened in 1978 were the company's first units in Arizona and New Mexico. At year-end, Mervyn's operated 51 stores.

Revenues	1978	1977
Mervyn's	$479,505,000	$369,055,000

Of the total, 45 are in California, three in Nevada, two in Arizona and one in New Mexico.

The merger with Mervyn's adds significantly to the Corporation's key strength of strategic and geographic balance. Mervyn's well-established market position in the rapidly growing Sun Belt, particularly in California, provides an excellent base for future expansion into the western and southwestern United States. The company's unique merchandise assortment—a popularly priced balance of nationally branded and private label apparel, accessories and household softgoods—as well as its merchandising approach of providing quality and fashion to the value-conscious family, are well suited to the retailing philosophy of Dayton Hudson Corporation.

Much of Mervyn's success has been the result of its highly effective central services. The primary example is the company's 350,000-square-foot distribution center in Hayward, California, which serves all 51 stores. Incoming merchandise is received, sorted, ticketed and re-packed for distribution to the appropriate stores—all within a three-day period. Built to handle a maximum of 54 stores, the two-year-old facility is reaching full capacity. Within the near future, Mervyn's will begin construction on a similar center in southern California.

Mervyn's plans to open a total of 10 stores in 1979—an additional 850,000 square feet of space.

The company will add three units in Arizona and three in California. Mervyn's fourth store in Nevada, an 85,000-square-foot unit in West Las Vegas, began operations in March. The store is the second in the Las Vegas market. In addition, Mervyn's will enter the Pacific Northwest with the opening of three stores in the Portland, Oregon, market.

Real Estate

Because we are convinced that focusing our efforts on retailing will provide our shareholders with an optimum return on investment over time, we have set forth an exciting and aggressive program of growth for our Retail business. Our plans have been developed to enable us to achieve a return on beginning shareholders' equity of 16% and an annual growth in earnings per share of 12% over the next five years.

An integral part of this strategic plan has been the redeployment of the investment in our Real Estate business. The sale of our nine wholly owned regional shopping centers to The Equitable Life Assurance Society of the United States in 1978 represented the first step in our plan to convert Real Estate assets into cash for use in future Retail expansion.

Under the terms of the transaction, Dayton Hudson received initial *cash* proceeds from the sale, after associated expenses, of $108 million. Additional cash will be forthcoming, based on the performance of the centers in 1978 and 1979, as evidenced by the $11.6 million gain recorded in the fourth quarter of 1978. As part of the agreement, an additional gain of approximately $20 million could be realized in 1979 based on the performance of the nine centers.

The second step of converting our Real Estate assets into cash was announced last fall. We are continuing to negotiate for the sale of two wholly owned shopping centers—the Meadows in Las Vegas, Nevada, and Columbia Mall in Grand Forks, North Dakota—and our interest in three other operating joint-venture projects.

Negotiations are also continuing for the sale of all of the Corporation's remaining interests in the Real Estate business, including our interest in another operating joint-venture project—Paradise Valley Mall in Phoenix, Arizona—and seven other joint-venture shopping centers which are at various early stages of development.

This decision to discontinue our Real Estate business means that in addition to the sale of the balance of these assets, the Corporation will sell its shopping center management and development business. We are studying the possibility of selling this service organization to certain members of the Dayton Hudson Properties management organization. We will retain the staff functions responsible for the construction and design of our Retail stores. The Real Estate Design and Construction function now reports directly to Dayton Hudson's President.

The organizational change has been made to support the future growth program of our Retail business and provides a pool of talented, experienced real estate executives to assist our operating companies in their growth plans.

Our Retail business has benefited from a professional approach to site selection, architectural development and construction management, and these disciplines will continue to be priority concerns for us. We are fortunate to have an experienced staff to support us in these important areas, as we anticipate the opening of more than 500 new stores over the next five years.

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Financial Review

The following discussion of Dayton Hudson's financial goals, policies, and planned capital expenditures relates to our Retail business (continuing operations).

Financial Goals

Dayton Hudson's primary financial objective is to provide its shareholders with an optimum return on investment over time through a combination of increased dividends and a higher stock price. To meet this objective, our aim is to grow and earn at a rate among the best in the industry.

Our specific goals are to earn a consistent return on beginning shareholders' equity (ROE) of at least 16% and sustain an annual growth in earnings per share of at least 12%. Return on beginning shareholders' equity for our Retail business was 17.4% in 1978, compared with 18.9% in 1977 and 17.6% in 1976. Excluding the impact of unusual expenses, ROE in 1978 would have exceeded that of 1977. Retail earnings per share increased 6% in 1978 after unusual expenses, and have increased at a compound annual growth rate of 27% over the past five years and 13% over the past ten.

Future achievement of our goals will depend upon our ability to:
- Continue to earn a high return on existing assets,
- Expand our existing high-return strategies, and
- Identify high-return strategies for future investments.

We believe return on investment (ROI) is the most important single measure of operating performance, and is the key to earnings growth and return on equity. ROI is the product of investment turnover and return on sales.

$$\text{ROI} = \frac{\text{Sales}}{\text{Investment}} \times \frac{\text{Earnings}}{\text{Sales}} = \frac{\text{Earnings}}{\text{Investment}}$$

After-tax earnings are adjusted to exclude financing costs. Investment is the sum of working capital and long-term assets, including the present value of all leases (capital *and* operating).

After-tax ROI for our Retail business was 12.1% in 1978, compared with 12.8% in 1977 and 11.7% in 1976. Excluding the impact of unusual expenses, 1978 ROI would have exceeded that of 1977.

	ROI	=	Investment Turnover	×	Return on Sales
1978	12.1%	=	3.26	×	3.72%
1977	12.8%	=	3.07	×	4.18%
1976	11.7%	=	2.89	×	4.04%

The following table shows the investment and the resulting return for 1978 and 1977.

Retail	(Millions of Dollars) 1978	1977
Net Earnings	$ 97.6	$ 91.7
Interest Expense After Tax	4.0	4.8
Interest Equivalent in Leases After Tax (a)	8.6	7.7
Earnings Before Financing Costs	$110.2	$104.2
Beginning of Year Investment:		
Working Capital (b)	$317.6	$303.6
Net Property and Equipment	379.7	317.2
Other Assets	6.1	7.1
Capital Leases	57.0	52.2
Present Value of Operating Leases	147.0	132.0
Total Investment	$907.4	$812.1
Return on Investment	12.1%	12.8%

(a) The interest equivalent in lease obligations is determined by assuming a 4.2% after-tax interest rate on beginning of year capital leases and the present value of operating leases.

(b) Current assets less current liabilities (excluding interest-bearing debt).

Return on investment is the primary financial tool used by Dayton Hudson to manage its business:

- **Performance Appraisal**
  The management of each operating company is evaluated and compensated first on the basis of its ability to meet an agreed-upon standard for ROI, and then — once that ability has been fully demonstrated — on the basis of the company's growth in earnings.
- **Capital Allocation**
  To receive capital for growth, an operating company must exceed its ROI standard. Additional criteria for allocating available capital include anticipated return on new investment, development of market position, the strength of the management team, and the quality of its strategic plan.
- **Capital Project Evaluation**
  New investment and capital projects are subject to a common discipline of analysis. Each project is expected to achieve a satisfactory ROI. Individual post-completion audits are performed to determine whether or not performance is up to expectations.

Financial Policies

The Corporation operates under clearly defined financial policies designed to maintain a strong, conservative capital structure and a strong "A" rating of our senior debt. Our long-term debt is currently rated A+/A and our commercial paper A-1/P-1 by Standard and Poor's and Moody's. Our policies are intended to provide maximum flexibility as to sources of funds and to reduce our cost of funds.

Capitalization Policies: Our target debt ratio, including capital leases and the present value of operating leases, is 40%. Management expects that the debt ratio will move toward that target during the next five years. As indicated in the following table, the

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Retail business ended 1978 with a debt ratio of 32%, compared with 38% in 1977 and 39% in 1976. This steady improvement is the result of internal cash flow and the proceeds of the shopping center sale by Dayton Hudson Properties exceeding our needs for funds. Intercompany advances from Dayton Hudson Properties to Retail will be a source of equity capital for the Retail business when our Real Estate business is liquidated.

Retail Capitalization

	(Millions of Dollars)		
	1978	1977	1976
Notes Payable	$ -0-	$ 5	$ 7
Long-Term Debt (including current portion)	101	123	120
Capital Leases (including current portion)	82	66	60
Present Value of Operating Leases	172	147	132
Total Debt and Equivalent	355	341	319
Intercompany Accounts — Long-Term	141	-0-	-0-
Deferred Items	9	7	8
Equity	621	559	485
Total Capitalization	$1126	$907	$812
Debt Ratio (Total Debt and Equivalent as a percentage of Total Capitalization)	32%	38%	39%

Financing Methods: The greater part of our Retail expansion has been financed with internally generated funds. Because we own the majority of our department and low-margin stores, depreciation provides a significant source of cash flow. We plan to finance over half of our expansion for the 1979-1983 period internally with retained earnings, depreciation and proceeds from the sale of Real Estate assets. We will continue to lease the majority of new specialty stores. We anticipate using a variety of debt sources to meet our needs for external funds.

Dividend Policy: It is our policy to make regular annual increases in dividends per share of Common Stock, consistent with earnings growth over time. A reduction in per share dividends would be considered only under severe economic or financial conditions.

Dividends paid in 1978 to holders of common shares totaled $1.45 per share, a 16% increase over 1977. The quarterly rate was increased to $.40 for the dividend payable December 8, 1978. The current annualized rate of dividends is $1.60 per share.

Capital Expenditures

Capital expenditures during 1978 reflected our continuing aggressive growth program, made possible by our strong financial position and competitive performance. Retail capital investment, including the present value of all new capital and operating leases, totaled $192 million in 1978 versus $130 million in 1977 and $99 million in 1976.

(Millions)	1978	1977	1976
Capital Expenditures	$136	$ 95	$66
Present Value of New Leases	56	35	33
Total	$192	$130	$99

For the 1979-1983 period, we plan to invest $1.3 billion in our existing Retail businesses. Our current plans contemplate the opening of approximately 15 department stores, 80 low-margin stores, 400 specialty stores and 50 Mervyn's stores. Nearly 75% of the total planned investment will support our three fastest growing companies: Target, Mervyn's, and B. Dalton.

Summary and Analysis of Operations

Earnings per share from continuing operations (Retail) increased 6% in 1978 (19% before unusual expenses), compared with an increase of 22% in 1977. The table below reconciles the change in earnings for 1978 versus 1977, and for 1977 versus 1976.

	1978	1977	1976
Earnings Per Share — Continuing (Retail)	$ 4.12	$3.89	$3.18
Earnings Per Share — Discontinued (Real Estate)	7.09	.27	.11
Consolidated Earnings Per Share	$11.21	$4.16	$3.29

Variance Analysis:	1978 vs 1977	1977 vs. 1976
Continuing Retail Operations		
Prior Year's Earnings Per Share	$3.89	$3.18
Change in Earnings Per Share due to:		
Sales Volume	.70	.54
Gross Margin Rate	.03	.08
Operating Expense Rate	(.13)	—
Start-up Expense	(.09)	(.04)
Corporate Expense	(.12)	(.02)
Income Tax Rate	.11	.04
Other Factors	.25	.11
Earnings before Unusual Expenses	$4.64	$3.89
Unusual Expenses	(.52)	—
Continuing Earnings Per Share	$4.12	$3.89
Discontinued Real Estate Operations		
Prior Year's Earnings Per Share	$ .27	$ .11
Changes in Earnings Per Share due to:		
Operating Income	(.29)	.05
Interest Income	.13	—
Gain from Property Sales (exclusive of sale of Shopping Centers)	(.05)	.02
Gain on sale of Shopping Centers	6.88	—
Joint Ventures	.01	.04
Other	.14	.05
Discontinued Earnings Per Share	$7.09	$ .27

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Significant Factors Affecting Earnings:

Continuing Operations (Retail)

Revenues in 1978 increased 18.7% from the prior year (17.4% on a comparable 52-week basis), compared with a 17.4% gain in 1977. From 1973 to 1978, the compound annual growth rate for total revenues was 15%. Part of the increase in revenues was due to inflation.

			1978 Increase		1977 Increase	
	1978	1977	All Stores	Comparable Stores	All Stores	Comparable Stores
	(Millions)					
Department	$1,172.3	$1,053.3	11.3%	4.5%	10.6%	6.7%
Low-Margin	1,055.1	858.8	22.9	10.0	18.4	8.1
Specialty	255.0	213.6	19.4	9.9	18.5	9.8
Mervyn's	479.5	369.0	29.9	18.5	37.7	23.0
	$2,961.9	$2,494.7	18.7%	8.9%	17.4%	9.5%

Comparable-store revenues exclude the first 12 months of operations of new stores. Comparable-store revenues increased 8.9% in 1978 versus 9.5% for both 1977 and 1976.

Productivity, as measured by revenues per square foot, increased 7.0% in 1978. The greatest increase was again achieved by low-margin stores. Specialty stores continue to operate at the highest productivity level.

	Revenues Per Square Foot*		
	1978	1977	1976
Department	$112	$106	$101
Low-Margin	142	130	120
Specialty	176	169	162
Mervyn's	136	129	121

*Average of beginning and end of year square feet

Gross Margin Rate increased in both 1978 and 1977, in large part due to improved merchandise mix emphasizing the higher margin departments and conversion to ownership from leasing in some departments at Mervyn's. Inventory shortage was also less than 1977, reflecting improved merchandising and inventory controls. The improvement in 1977 was somewhat tempered by a more competitively promotional retail environment.

Operating Expenses increased slightly as a percentage of sales to 28% in 1978, compared with 27.7% in 1977 and 1976. The relationship of operating expenses to sales has been used as an indicator of the relative amount of each sales dollar that is required for occupancy expense, payroll, advertising, and other expenses directly supporting Retail operations. Higher payroll costs, including the effect of the higher minimum wage, plus an increase in the provision for doubtful accounts caused some of the increase in this year's rate. The ability of the Corporation to maintain its operating expense rates in prior years, and realize only a slight increase in 1978, reflects the increasing relative size of Target and B. Dalton, which typically incur lower operating expenses per sales dollar than the department stores.

- Maintenance and repairs expense increased $1.7 million in 1978 and $2.4 million in 1977. The higher increase in 1977 resulted from additional maintenance programs in the department store group and Mervyn's.
- Depreciation and amortization expense increased $3.2 million in 1978 and $4.4 million in 1977 due to new store openings. The 1978 increase was partially offset by lower depreciation ($1.9 million) due to a change in the Corporation's estimate of remaining depreciable lives, made as a result of a settlement with the IRS in 1977.
- Taxes other than income taxes increased $4.9 million in 1978 and $6.6 million in 1977 because of higher payroll taxes resulting from additional employees and increased social security taxes.
- Rental expense increased 28% in 1978 and 22% in 1977 due to new store leases and higher percentage rentals resulting from increases in mature store sales.
- Advertising expense increased $9.4 million in 1978 and $9.5 million in 1977, principally reflecting new store openings in both years.
- The provision for doubtful accounts increased 44% in 1978 and 35% in 1977, reflecting a greater amount of credit sales and extended payment terms used by department store customers.

Start-up Expenses were $19 million in 1978, $14.5 million in 1977 and $12.5 million in 1976. These increases reflect the higher rate of expansion beginning in 1976 and continuing through 1978. In 1978, the Corporation opened five department stores, nine low-margin stores, 62 specialty stores, and nine Mervyn's stores — a net addition of 2,533,000 square feet. This compares with a net addition of 2,020,000 square feet of Retail space in 1977.

	End of 1978		End of 1977	
Department Stores	Stores	Space*	Stores	Space*
Hudson's	15	5,481	14	5,277
Dayton's	15	3,047	13	2,825
Diamonds	9	1,112	7	862
Lipmans	7	671	7	674
John A. Brown	5	488	5	488
Total	51	10,799	46	10,126
Low-Margin Stores				
Target	67	6,917	59	6,117
Lechmere	6	992	5	882
Total	73	7,909	64	6,999
Specialty Stores				
Jewelers	45	181	43	176
B. Dalton	357	1,338	298	1,112
Team**	11	29	23	58
Total	413	1,548	364	1,346
Mervyn's	51	3,902	42	3,154
Total Retail Stores	588	24,158	516	21,625

*Thousands of square feet (excluding office, warehouse and vacant space).
**Includes only company-owned stores.

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In 1979, the Corporation plans to open one department store, 13 low-margin stores, 79 specialty stores and 10 Mervyn's stores, for a total of approximately 2.5 million square feet of additional Retail space.

Corporate Expense was $18.8 million in 1978, $13.2 million in 1977 and $12.5 million in 1976. The 1978 and 1977 increases were due to higher Corporate staff expenses and charitable contributions. The 1978 increase also includes a $1.8 million provision for satisfaction of a lawsuit against Team Central, Incorporated.

Income Tax Rate for Retail was 50.9% in 1978 and 51% in 1977. Exclusive of the effect of unusual expenses, this year's rate was 49.8%. The Corporation received partial benefit in 1978 from the lower Federal income tax rate instituted at the beginning of calendar year 1979. In addition, investment tax credit as a percent of pre-tax income was larger in 1978 than in 1977.

Other factors affecting net income include the following items:

- FASB #13 — Accounting for Leases — has been retroactively implemented. Minimum rental expense in 1978 and 1977 relating to leases capitalized under FASB #13 has been eliminated and replaced with interest and depreciation. The increased expense in 1978 and 1977 was due primarily to capitalizing certain of Mervyn's new leases.
- Interest expense declined in 1978 due to lower debt levels, and increased in 1977 due to higher short-term borrowings needed by Mervyn's to finance its expansion.
- Finance charge revenue (carrying charges on customer receivable balances) increased by 22% in 1978 and 24% in 1977.

Unusual Expenses in 1978 included $2.9 million of merger fees resulting from the business combination with Mervyn's, a $13.2 million provision for loss on the closing and demolition of Hudson's downtown store, and $3.7 million of expense provided for the disposition of Team Central and Lipmans. These unusual expenses decreased 1978 net income by $.52 per share.

Discontinued Real Estate Operations

In May 1978, the Corporation closed the sale of nine wholly owned regional shopping centers to The Equitable Life Assurance Society of the United States. The sale resulted in a gain of $6.88 per share in 1978, $.49 of which was recognized in the fourth quarter. The fourth quarter gain resulted from performance of the centers, which exceeded certain predetermined standards. In February 1979, the Board of Directors approved a formal plan for the disposition of the Corporation's remaining Real Estate interests which are not now directly employed or to be employed in its Retail operations. These remaining interests include three wholly owned shopping centers and joint venture interests in eleven others.

- The significant decrease in income from operating properties in 1978 reflects the sale of the nine wholly owned shopping centers in May 1978.
- Interest income in 1978 resulted from the short-term investment of a portion of the proceeds of the shopping center sale.
- Gains from property sales in 1977 increased due to collections on prior year installment sales and disposals of certain land not needed in the business. The results of the joint venture operations over the past two years have improved as a result of land sales plus an improving operating profit.

Common Stock Price and Dividend Data

Dayton Hudson Corporation Common Stock is listed on the New York Stock Exchange with the symbol *DH,* and abbreviated in newspaper listings as *DaytHd.* The number of Dayton Hudson shareholders increased 22% to 12,804 in 1978 from 10,474 in 1977, due principally to the addition of former shareholders of Mervyn's who received Dayton Hudson shares in exchange for Mervyn's shares.

Fiscal Quarter	Common Stock Price Range 1978 High	1978 Low	1977 High	1977 Low	Quarterly Dividend Paid Per Share 1978	1977
First	$42⅜	$35¼	$36¾	$30¾	$ .35	$ .30
Second	44¼	36⅜	35	29½	.35	.30
Third	43	35⅝	40½	34½	.35	.30
Fourth	39¼	33¼	43⅞	37	.40	.35
Year	$44¼	$33¼	$43⅞	$29½	$1.45	$1.25

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Results of Operations

Dayton Hudson Corporation and Subsidiaries

(Thousands of Dollars, Except Per Share Data)

RETAIL
Continuing Operations

	1978	1977
REVENUES		
Net retail sales, including leased departments and carrying charges (Note D)	$2,959,743	$2,492,870
Rental revenue	2,141	1,854
	2,961,884	2,494,724
COSTS AND EXPENSES		
Cost of retail sales, buying and occupancy	2,055,362	1,731,586
Selling, publicity and administrative	539,474	445,229
Depreciation and amortization	34,401	31,159
Rental expense	43,530	33,942
Interest expense	8,207	9,890
Interest and depreciation on capital leases (Note G)	12,023	10,425
Taxes other than income taxes	50,237	45,334
	2,743,234	2,307,565
EARNINGS BEFORE UNUSUAL EXPENSES AND INCOME TAXES	218,650	187,159
UNUSUAL EXPENSES (Note A)	19,750	—
EARNINGS BEFORE INCOME TAXES	198,900	187,159
INCOME TAXES (Note Q)		
Current	96,381	82,492
Deferred	4,880	12,957
	101,261	95,449
NET EARNINGS	$ 97,639	$ 91,710
NET EARNINGS PER SHARE	$ 4.12	$ 3.89

REAL ESTATE
Discontinued Operations

OPERATING PROPERTIES

Rental and other operating revenue ....

Interest income ....

EXPENSES AND OTHER INCOME

Operating expenses ....

Interest expense:

Operating ....

Development ....

Other ....

Depreciation and amortization ....

Development expense ....

Net gain from property sales, exclusive of gain reported below ....

Other, net ....

Gain from sale of shopping centers (Note A) ..

EARNINGS BEFORE EQUITY IN EARNINGS (LOSS) OF JOINT VENTURES AND INCOME TAXES ....

EQUITY IN EARNINGS (LOSS) OF JOINT VENTURES (Note F) ....

EARNINGS BEFORE INCOME TAXES ....

INCOME TAXES (Note Q)

Current ....

Deferred ....

NET EARNINGS ....

NET EARNINGS PER SHARE ....

See accompanying Summary of Accounting Policies and Notes to Financial Statements.

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1978	1977
$ 19,350	$43,607
6,239	—
25,589	43,607
8,747	18,928
3,578	8,104
1,130	190
217	296
2,328	5,717
2,859	1,464
(1,974)	(4,970)
457	411
17,342	30,140
241,827	—
250,074	13,467
(254)	(1,040)
249,820	12,427
89,379	7,288
(6,825)	(1,087)
82,554	6,201
$167,266	$ 6,226
$ 7.09	$ .27

CONSOLIDATED

	1978	1977
REVENUES		
Net retail sales, including leased departments and carrying charges	$2,959,743	$2,492,870
Rental revenue	2,141	1,854
	2,961,884	2,494,724
COSTS AND EXPENSES		
Cost of retail sales, buying and occupancy	2,055,362	1,731,586
Selling, publicity and administrative	539,474	445,229
Depreciation and amortization	34,401	31,159
Rental expense	43,530	33,942
Interest expense	8,207	9,890
Interest and depreciation on capital leases (Note G)	12,023	10,425
Taxes other than income taxes	50,237	45,334
	2,743,234	2,307,565
EARNINGS FROM CONTINUING OPERATIONS BEFORE UNUSUAL EXPENSES AND INCOME TAXES	218,650	187,159
UNUSUAL EXPENSES (Note A)	19,750	—
EARNINGS BEFORE INCOME TAXES	198,900	187,159
INCOME TAXES (Note Q)		
Current	96,381	82,492
Deferred	4,880	12,957
	101,261	95,449
NET EARNINGS FROM CONTINUING OPERATIONS	97,639	91,710
DISCONTINUED OPERATIONS, net of income taxes (Note B)		
Net gain from Real Estate property sales	163,775	2,485
Other Real Estate operations	3,491	3,741
NET EARNINGS FROM DISCONTINUED OPERATIONS	167,266	6,226
NET EARNINGS	$ 264,905	$ 97,936
NET EARNINGS PER SHARE:		
Continuing operations	$ 4.12	$ 3.89
Discontinued operations	7.09	.27
	$ 11.21	$ 4 16

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Statements of Financial Position

Dayton Hudson Corporation and Subsidiaries

(Thousands of Dollars)

RETAIL
Continuing Operations

ASSETS	1978 February 3, 1979	1977 January 28, 1978
CURRENT ASSETS		
Cash	$ 25,449	$ 18,890
Short-term investments	36,007	34,959
Accounts receivable (Note D)		
Thirty day accounts	2,885	2,584
Deferred payment accounts	464,302	400,517
Other accounts	19,272	12,271
Less allowance for losses	(17,609)	(12,788)
	468,850	402,584
Merchandise inventories (Note E)	393,437	337,347
Other current assets	12,750	9,388
TOTAL CURRENT ASSETS	936,493	803,168
INVESTMENTS AND OTHER ASSETS	5,696	6,088
PROPERTY AND EQUIPMENT (Note J)		
Land	70,158	59,773
Buildings and improvements	402,908	352,121
Fixtures and equipment	171,481	139,287
Construction in progress	41,242	31,141
Accumulated depreciation	(213,602)	(202,660)
	472,187	379,662
LEASED PROPERTY UNDER CAPITAL LEASES, net of accumulated amortization (Note G)	70,888	56,976
	$1,485,264	$1,245,894

LIABILITIES AND SHAREHOLDERS' INVESTMENT	1978	1977
CURRENT LIABILITIES		
Notes payable	$ —	$ 4,497
Accounts payable (Note I)	246,971	244,039
Taxes other than income taxes	37,826	35,757
Accrued liabilities	104,629	74,531
Income taxes, currently payable	62,618	42,971
Intercompany accounts	—	20,741
Deferred income taxes — installment sales (Note Q)	79,533	67,461
Current portion of long-term debt and capital lease obligations	11,715	10,466
TOTAL CURRENT LIABILITIES	543,292	500,463
INTERCOMPANY ACCOUNTS — LONG-TERM (Note J)	141,311	—
LONG-TERM DEBT (Note J)	94,310	116,782
LONG-TERM CAPITAL LEASE OBLIGATIONS (Note G)	76,824	61,956
DEFERRED INCOME TAXES AND OTHER LONG-TERM LIABILITIES (Notes K and Q)	8,702	7,160
COMMITMENTS AND CONTINGENCIES (Notes G and L)	—	—
SHAREHOLDERS' INVESTMENT (Note M)	620,825	559,533
	$1,485,264	$1,245,894

See accompanying Summary of Accounting Policies and Notes to Financial Statements.

REAL ESTATE
Discontinued Operations

ASSETS
CURRENT ASSETS
Cash
Short-term investments
Accounts receivable
Less allowance for losses
Other current assets
TOTAL CURRENT ASSETS
INVESTMENTS AND OTHER ASSETS (Note F)
PROPERTY AND EQUIPMENT (Note J)
Land
Buildings and improvements
Fixtures and equipment
Construction in progress
Accumulated depreciation

LIABILITIES AND SHAREHOLDERS' INVESTMENT
CURRENT LIABILITIES
Accounts payable
Taxes other than income taxes
Accrued liabilities
Income taxes, currently payable
Intercompany accounts
Current portion of long-term debt
TOTAL CURRENT LIABILITIES
INTERCOMPANY ACCOUNTS — LONG-TERM (Note J)
LONG-TERM DEBT (Note J)
DEFERRED INCOME TAXES AND OTHER CREDITS (Notes K and Q)
COMMITMENTS AND CONTINGENCIES (Note L)
SHAREHOLDERS' INVESTMENT (Note M)

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	1978 February 3, 1979	1977 January 28, 1978
	$ 2	$ 3
	61,000	—
	42,853	15,507
	(203)	(336)
	42,650	15,171
	330	289
	103,982	15,463
	2,163	10,450
	9,965	25,281
	38,001	151,773
	1,025	2,501
	930	24,521
	(3,840)	(64,509)
	46,081	139,567
	$152,226	$165,480
	$ 2,753	$ 6,452
	2,709	10,443
	3,852	4,875
	60,023	5,042
	—	(20,741)
	257	2,662
	69,594	8,733
	(141,311)	—
	28,554	127,299
	7,849	9,174
	—	—
	187,540	20,274
	$152,226	$165,480

CONSOLIDATED

ASSETS	1978 February 3, 1979	1977 January 28, 1978
CURRENT ASSETS		
Cash	$ 25,449	$ 18,890
Short-term investments	36,007	34,959
Accounts receivable (Note D)		
Thirty day accounts	2,885	2,584
Deferred payment accounts	464,302	400,517
Other accounts	19,272	12,271
Less allowance for losses	(17,609)	(12,788)
	468,850	402,584
Merchandise inventories (Note E)	393,437	337,347
Current assets of discontinued segment (Note B)	103,982	15,463
Other current assets	12,750	9,388
TOTAL CURRENT ASSETS	1,040,475	818,631
INVESTMENTS AND OTHER ASSETS	5,696	6,088
NON-CURRENT ASSETS OF DISCONTINUED SEGMENT (Note B)	48,244	150,017
PROPERTY AND EQUIPMENT (Note J)		
Land	70,158	59,773
Buildings and improvements	402,908	352,121
Fixtures and equipment	171,481	139,287
Construction in progress	41,242	31,141
Accumulated depreciation	(213,602)	(202,660)
	472,187	379,662
LEASED PROPERTY UNDER CAPITAL LEASES, net of accumulated amortization (Note G)	70,888	56,976
	$1,637,490	$1,411,374
LIABILITIES AND SHAREHOLDERS' INVESTMENT		
CURRENT LIABILITIES		
Notes payable	$ —	$ 4,497
Accounts payable (Note I)	246,971	244,039
Taxes other than income taxes	37,826	35,757
Accrued liabilities	104,629	74,531
Income taxes, currently payable	62,618	42,971
Deferred income taxes — installment sales (Note Q)	79,533	67,461
Current portion of long-term debt and capital lease obligations	11,715	10,466
Current liabilities of discontinued segment (Note B)	69,594	29,474
TOTAL CURRENT LIABILITIES	612,866	509,196
LONG-TERM LIABILITIES OF DISCONTINUED SEGMENT (Note B)	36,403	136,473
LONG-TERM DEBT (Note J)	94,310	116,782
LONG-TERM CAPITAL LEASE OBLIGATIONS (Note G)	76,824	61,956
DEFERRED INCOME TAXES, CREDITS AND OTHER LONG-TERM LIABILITIES (Notes K and Q)	8,702	7,160
COMMITMENTS AND CONTINGENCIES (Notes G and L)	—	—
SHAREHOLDERS' INVESTMENT (Note M)	808,365	579,307
	$1,637,490	$1,411,374

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Statements of Changes in Financial Position

Dayton Hudson Corporation and Subsidiaries

(Thousands of Dollars)

RETAIL
Continuing Operations

	1978	1977
FUNDS PROVIDED BY		
Continuing Operations:		
Net earnings	$ 97,639	$ 91,710
Items not affecting working capital:		
Depreciation and amortization	34,401	31,159
Depreciation on capital leases	6,020	5,221
Decrease in non-current deferred income taxes	(7,015)	(1,293)
Provision for loss on store closing	13,200	—
Other items	54	72
Funds provided by operations	144,299	126,869
Increase in long-term intercompany liabilities	141,311	—
Obligations incurred under capital leases	19,989	9,968
Disposals of property and equipment	2,594	1,286
Proceeds from exercise of stock options	2,376	2,853
Other, net	2,343	832
Increase in long-term debt	812	15,032
	$313,724	$156,840
FUNDS USED FOR		
Additions to property and equipment	$136,111	$ 94,915
Dividends (Note M)	38,723	20,218
Additions to leased property under capital leases	19,989	9,968
Mortgage debt of shopping centers sold	12,903	—
Prepayments on long-term debt	3,481	3,837
Scheduled reductions of long-term debt	6,900	6,094
Reduction in lease obligations	5,121	4,602
Increase in working capital	90,496	17,206
	$313,724	$156,840
INCREASES (DECREASES) IN COMPONENTS OF WORKING CAPITAL		
Cash	$ 6,559	$ 8,677
Short-term investments	1,048	(28,737)
Accounts receivable	66,266	78,405
Merchandise inventories	56,090	59,212
Other current assets	3,362	(4,231)
Increase in current assets	133,325	113,326
Notes payable	(4,497)	(2,703)
Accounts payable	2,932	47,450
Accrued expenses and other	44,239	35,158
Income taxes, currently payable	19,647	8,448
Current portion of long-term debt and capital lease obligations	1,249	(455)
Intercompany accounts	(20,741)	8,222
Increase in current liabilities	42,829	96,120
Net increase	$ 90,496	$ 17,206

See accompanying Summary of Accounting Policies and Notes to Financial Statements.

REAL ESTATE
Discontinued Operations

FUNDS PROVIDED BY

Operations:

Net earnings

Items not affecting working capital:

Depreciation and amortization

Equity in loss of joint ventures

Decrease in non-current deferred income taxe

Gain on sale of shopping centers, net of incom

Other items

Funds provided by operations

Principal payments on long-term debt

Funds (used) provided after debt service

Sale of shopping centers (Note A):

Cash proceeds, debt and additional earnout

Income taxes applicable to gain

Mortgage debt

Increase in long-term advances to Retail

Other

Funds provided by sale

Increase in long-term debt

Disposals of property and equipment, exclusive c

Increase (decrease) in deferred income

(Increase) decrease in long-term receivables

FUNDS USED FOR

Increase in long-term intercompany advances (exclusive of sale of shopping centers)

Additions to property and equipment

Mortgages assumed by purchasers of office prop and prepayments on land contracts

Investments in and advances to joint ventures

Increase in other working capital items, net

Other, net

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	1978	1977
	$167,266	$ 6,226
	2,328	5,717
	254	1,040
s	(7,002)	(1,087)
e taxes	(162,371)	—
	137	74
	612	11,970
	(3,157)	(3,539)
	(2,545)	8,431
	331,941	—
	(79,456)	—
	(109,882)	—
	(12,903)	—
	(3,578)	—
	126,122	—
	11,813	17,105
f shopping centers	16,702	10,041
	3,237	(504)
	5,326	(1,857)
	$160,655	$33,216
	$128,408	$ —
	9,797	27,010
erties		
	1,687	1,664
	(3,605)	(417)
	25,174	2,837
	(806)	2,122
	$160,655	$33,216

CONSOLIDATED

	1978	1977
FUNDS PROVIDED BY		
Continuing Operations:		
Net earnings	$ 97,639	$ 91,710
Items not affecting working capital:		
Depreciation and amortization	34,401	31,159
Depreciation on capital leases	6,020	5,221
Decrease in non-current deferred income taxes	(7,015)	(1,293)
Provision for loss on store closing	13,200	—
Other items	54	72
Funds provided by continuing operations	144,299	126,869
Funds provided by discontinued Real Estate operations	612	11,970
Total funds provided by operations	144,911	138,839
Sale of shopping centers (Real Estate)	126,122	—
Obligations incurred under capital leases	19,989	9,968
Increases in long term liabilities of discontinued segment, net of shopping center sale	12,611	12,147
Disposals of property and equipment	2,594	1,286
Proceeds from exercise of stock options	2,376	2,853
Other, net	2,343	832
Increase in long-term debt	812	15,032
	$311,758	$180,957
FUNDS USED FOR		
Additions to property and equipment	$136,111	$ 94,915
Dividends (Note M)	38,723	20,218
Additions to leased property under capital leases	19,989	9,968
Prepayments on long-term debt	3,481	3,837
Scheduled reductions of long-term debt	6,900	6,094
Reduction in lease obligations	5,121	4,602
Increase (decrease) in non-current assets of discontinued segment, net of shopping center sale	(16,721)	20,117
Increase in working capital	118,154	21,206
	$311,758	$180,957
INCREASES (DECREASES) IN COMPONENTS OF WORKING CAPITAL		
Cash	$ 6,559	$ 8,677
Short-term investments	1,048	(28,737)
Accounts receivable	66,266	78,405
Merchandise inventories	56,090	59,212
Other current assets	3,362	(4,231)
Current assets of discontinued segment	88,519	5,414
Increase in current assets	221,844	118,740
Notes payable	(4,497)	(2,703)
Accounts payable	2,932	47,450
Accrued expenses and other	44,239	35,158
Income taxes, currently payable	19,647	8,448
Current portion of long-term debt and capital lease obligations	1,249	(455)
Intercompany accounts	—	8,222
Current liabilities of discontinued segment	40,120	1,414
Increase in current liabilities	103,690	97,534
Net increase	$118,154	$ 21,206

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Statement of Shareholders' Investment

Dayton Hudson Corporation and Subsidiaries

(Thousands of Dollars)

	RETAIL Continuing Operations	REAL ESTATE Discontinued Operations	CONSOLIDATED				
			Total	Preferred Stock	Common Stock	Additional Paid-In Capital	Retained Earnings
BALANCE JANUARY 29, 1977 as previously reported	$489,100	$ 14,048	$503,148	$542	$19,650	$56,981	$425,975
Effect of capitalization of leases (Note G)	(3,912)		(3,912)				(3,912)
	485,188	14,048	499,236	542	19,650	56,981	422,063
Net earnings	91,710	6,226	97,936				97,936
Dividends:							
Common Stock	(19,925)		(19,925)				(19,925)
Preferred Stock	(293)		(293)				(293)
Conversions of Preferred Stock				(20)	5	15	
Stock options	2,853		2,853		116	2,737	
Stock split in the form of a dividend					3,775	(3,775)	
BALANCE JANUARY 28, 1978 (Note M)	559,533	20,274	579,807	522	23,546	55,958	499,781
Net earnings	97,639	167,266	264,905				264,905
Dividends:							
Common Stock	(38,388)		(38,388)				(38,388)
Preferred Stock	(335)		(335)				(335)
Conversions of Preferred Stock				(57)	15	42	
Stock options	2,376		2,376		91	2,285	
BALANCE FEBRUARY 3, 1979 (Note M)	$620,825	$187,540	$808,365	$465	$23,652	$58,285	$725,963

See accompanying Summary of Accounting Policies and Notes to Financial Statements

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Summary of Accounting Policies and Notes to Financial Statements

Dayton Hudson Corporation and Subsidiaries

Fiscal Years Ended February 3, 1979 and January 28, 1978

(Dollar amounts in thousands, except Note R)

Dayton Hudson Corporation follows generally conservative accounting policies. The following is a description of those policies.

Consolidation. The financial statements include the accounts of Dayton Hudson Corporation and subsidiaries, all of which are wholly owned, including the Company's newly acquired subsidiary, Mervyn's (see Note A), after elimination of intercompany balances and transactions.

Financial Data by Line of Business. Dayton Hudson Corporation operates its Retail business through department, low margin, specialty and Mervyn's stores. Through its Real Estate operations, which are being discontinued (see Note B), it develops and manages regional shopping centers and other commercial properties. The Company also owned nine shopping centers which it sold on May 18, 1978 (see Note A).

Line of Business financial statements have been included in 1978 to illustrate the significant impact of Real Estate transactions. They will not be presented in future periods because it is anticipated that Real Estate operations will cease in 1979.

The following methods of allocating costs and expenses employed to prepare the separate Line of Business financial statements had significantly greater impact prior to the sale of the shopping centers, since legal entities are not exclusively Retail or Real Estate. After the sale, these allocations are no longer necessary, except that four retail department store facilities still owned by Real Estate are considered Retail property. Operating costs and expenses attributable to these properties are also considered part of the Retail Line of Business.

1. Assets, liabilities, revenues and expenses specifically identifiable as Retail or Real Estate are so designated. Short term investments of $61,000 have been retained in Real Estate in anticipation of satisfaction of income tax liabilities arising from the shopping center sale.
2. Shopping center property, including related depreciation, owned by Real Estate and utilized by the Company's department stores was allocated to the applicable Retail stores on the basis of the percentage of gross area occupied by the stores. The common mall areas, heating, ventilating and air conditioning facilities of the shopping centers were considered Real Estate properties. Parking lot area was allocated on the basis of leasable space in the center, a practice consistent with industry standards.
3. Secured debt and the related interest expense was allocated on the same basis as the property pledged as collateral on the debt. Unsecured long-term debt has been assigned to Retail.
4. Property taxes were allocated on the basis of gross leasable area, in general accordance with terms of leases with shopping center tenants.
5. Separate income tax provisions are computed for each line of business. Tax benefits and items that require specific treatment in the Consolidated Federal income tax return are assigned to the originating line of business. Deferred income taxes have been assigned to the Retail or Real Estate line of business based on the assets or liabilities associated with those deferred taxes.
6. Applicable Corporate Office expenses are allocated based on assets, sales and payroll dollars.

The Real Estate line of business has followed the installment sales method for recording sales of property.

The detailed segment of business information on the department, low-margin, specialty and Mervyn's segments set forth in "Five-Year Segment of Business Comparisons" is incorporated herein by reference.

Accounts Receivable and Allowance for Losses. Generally the Company's policy is to write off Retail accounts receivable if any portion of the balance is more than 12 months past due, or when the scheduled payment has not been received for six consecutive months. The allowance for losses for uncollectible customer accounts receivable is based upon historical bad-debt experience and current agings of the accounts. Certain accounts due beyond one year are classified as current in accordance with industry practice (see Note D).

Inventories. Inventories and related cost of sales are accounted for principally by the retail inventory method using primarily the last-in, first-out (LIFO) basis (see Note E).

Joint Venture Investments. The Company accounts for its investments in joint ventures using the equity method, on a one-month lag basis. All the joint ventures of the Real Estate subsidiaries have adopted a calendar year as their fiscal year.

Property and Equipment. Property and equipment is carried at cost less accumulated depreciation.

Depreciation is computed using the straight-line method for financial reporting purposes and accelerated methods for tax purposes except in the case of leased property under capital leases where normal rent expense is deducted for tax purposes.

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The following policies are used in computing depreciation:

Land improvements	20 years
Buildings and improvements	8 to 55 years
Fixtures and equipment	4 to 8 years
Leasehold improvements	Lease term, or useful life of asset, whichever is less
Tenant allowances	18 or 24 years
Leased property under capital leases	Lease term or useful life of asset if ownership is transferred

Beginning with first quarter of fiscal 1978, the Company changed its estimate of remaining depreciable lives used for certain of its real property. The change was made to conform the depreciable lives of these assets to those used in the Company's Consolidated Federal income tax return, which were revised as a result of the settlement of an Internal Revenue Service audit in 1977. The effect of the change on the results of operations for fiscal 1978 and future years is not considered material.

Expenditures for maintenance and repairs are charged to expense. Betterments and major renewals are capitalized and charged to the appropriate property account. The cost of assets retired or otherwise disposed of and the related allowances for depreciation and amortization are eliminated from the accounts in the year of disposal and the resulting gain or loss is credited or charged to profit and loss.

Real Estate capitalizes real property taxes and certain other costs, exclusive of interest, associated with the construction or development of a project. The Retail segment expenses real property taxes and interest.

Costs capitalized by Real Estate are classified as construction in progress until the project becomes operational, at which time the accumulated project costs are transferred to operating property categories and depreciated over the appropriate life. Preliminary development expenses are charged to current operations until there is a commitment for construction of a project. Interest and real estate taxes related to undeveloped land are expensed as incurred.

Income Taxes. Gross profit on Retail installment sales is recognized for financial reporting purposes when the sales are recorded. For income tax purposes the installment method of reporting profit on installment sales is used.

Deferred income taxes arising from Retail installment sales are included in the Statements of Financial Position as a current liability. Other deferred income taxes result principally from accelerated depreciation methods and the effect of capital leases.

The Company and its subsidiaries file Consolidated Federal and certain state income tax returns. The majority of the state income tax returns are filed on a separate company basis.

The investment tax credit reduces income taxes in the year the property is placed in service.

Other Costs. Expenses incurred in connection with obtaining long-term financing are amortized over the term of the related debt.

Costs incurred as lessor in acquiring new tenants of leased facilities are capitalized and amortized over the term of the lease.

Interim Reporting. The unaudited interim financial data furnished in Note R has been prepared based on accounting policies applicable to annual data. In addition, certain accounting policies are applicable only to the preparation of interim data, the most significant of which are as follows:

1. Costs associated with the opening of new stores each fiscal year are provided for ratably over the year.
2. Real estate taxes, bonuses, contributions, professional fees, and pension plan expense are provided for throughout the year based on anticipated annual amounts.
3. Contingent rental expense is incurred throughout the year as a percentage of sales in excess of a ratable allocation of stipulated annual sales amounts below which no percentage rents would be required.
4. The estimated annual provision for LIFO expense is allocated to interim periods based on monthly sales.
5. Income taxes are provided on interim earnings using an anticipated effective annual tax rate.

Employee Benefits. The Company and its subsidiaries have defined benefit retirement plans covering substantially all employees. Pension costs are paid to the plans as accrued by the Company. Costs with respect to the plans are actuarially computed using the "Frozen Initial Liability Aggregate Cost Method—Modified." Under this method, unfunded costs and actuarial gains and losses are spread over future periods ranging from 15 to 37 years.

In addition, a Savings and Stock Purchase Plan is made available to substantially all of the Company's employees, exclusive of Mervyn's, who meet the eligibility requirements (primarily based on age and length of service). Employees can contribute up to a maximum of 10% of their current cash compensation to the plan. Under this plan the Company contributes 50 cents for each dollar deposited by the employee up to a maximum of 2½% of the participant's current cash compensation. Employees become partially vested after participating in the plan for two years. The employee is fully vested after six years. Mervyn's eligible employees participate in a Supplemental Retirement Plan (defined contribution profit-sharing plan) supported by annual contributions of the Company. The Supplemental Retirement Plan continues in effect although no new persons can become participants nor will contributions be made in future years.

Per Share Data. Net earnings per share, Consolidated and Retail, have been computed after provision for dividends on Preferred Stock, based upon the weighted average number of common

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shares outstanding retroactively adjusted for shares issued in conjunction with the Mervyn's merger based on the historical number of average outstanding shares of Mervyn's common stock (adjusted for a two-for-one stock split in 1977 effected in the form of a 100% stock dividend) during the respective periods. Per share amounts for Real Estate have been computed based on net earnings of Real Estate operations without provision for dividends on Preferred Stock. Exercise of stock options and conversion of Preferred Stock would not have a materially dilutive effect on earnings per share.

Fiscal Year. The Company's 1978 fiscal year ended on the Saturday closest to January 31 (February 3, 1979) and included 53 weeks, except for 52 weeks for Mervyn's whose fiscal year ended on the last Sunday in January (January 28, 1979). The Company's 1977 fiscal year ended on January 28, 1978 and included 52 weeks.

Reclassification of Accounts. Certain account balances of prior years have been reclassified to conform with current classifications. None of these reclassifications had an effect on net earnings.

Restatement. All financial information presented herein includes the account balances and results of operations of Mervyn's from the beginning of the periods to give effect to the Mervyn's merger on May 28, 1978 which was accounted for as a pooling of interests. Adjustments and reclassifications have been made for an inter-company transaction and to establish consistency of account classification between the two companies.

The Company retroactively implemented the provisions of FASB #13 "Accounting for Leases" by restating 1977 Results of Operations and the Statement of Financial Position at January 28, 1978 (see Note G). Quarterly data for 1978 and 1977 has been restated accordingly (see Note R). The cumulative impact on retained earnings has been included in the Statement of Shareholders' Investment as an adjustment to the January 29, 1977 balance.

NOTE A. SIGNIFICANT TRANSACTIONS

Business Combination

Shareholders of the Company and Mervyn's, a retail chain based in Hayward, California, approved an agreement that provided for the merger of a wholly owned subsidiary of the Company with Mervyn's. The merger was effective May 28, 1978 and has been accounted for as a pooling of interests involving the combining of the account balances of the two companies and the exchange of approximately 7,553,000 shares of the Company's Common Stock for all outstanding shares of Mervyn's. The accompanying financial statements reflect the combination of the two companies.

Selected operating data of the separate companies for the interim period nearest the combination date, and of the Company for 1977 are as follows:

	First Quarter Ended (Unaudited)			
	April 29, 1978 Dayton Hudson	April 30, 1978 Mervyn's	Reclassification and Adjustments	As Restated*
Revenues	$481,252	$83,291	$2,452	$566,995
Gross Profit	$141,698	$28,734	—	$170,432
Net Earnings				
From Continuing Operations	$ 8,566	$ 3,071	$ (399)	$ 11,238
From Discontinued Operations	1,093	—	(163)	930
Consolidated	$ 9,659	$ 3,071	$ (562)	$ 12,168
Dividends	$ 5,671	—	—	$ 5,671

*Includes restatement for leases and Mervyn's start-up costs (Note R).

	1977
Revenues:	
Dayton Hudson, as previously reported	$2,125,669
Mervyn's, as previously reported (after reclassification)	369,055
As reported herein	$2,494,724
Net earnings:	
Dayton Hudson, as previously reported	$ 80,901
Mervyn's, as previously reported	17,768
	98,669
Lease capitalization restatement (Note G)	(733)
As reported herein	$ 97,936

Sale of Shopping Centers

On May 18, 1978, the Company closed the sale of nine wholly owned regional shopping centers to The Equitable Life Assurance Society of the United States. Under terms of the shopping center sale, the Company received payment during 1978 of $185,000 in cash, and the Equitable acquired title to the properties subject to $122,800 in existing long-term debt and assumed $4,500 of other liabilities. At the date of sale the carrying value of the nine centers was $84,800.

The transaction resulted in a 1978 gain (after expenses of $5,200 and associated income taxes of $79,456) of $162,371 or $6.88 per share. The gain includes $11,606 which was realized after May 18

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as a result of the centers' performance exceeding certain predetermined standards. An additional gain may also be realized in 1979 of approximately $20,000 in accordance with the terms of the agreement.

Real Estate Results of Operations for 1978 and 1977 include $11,595 and $41,200, respectively, of revenues and $1,700 and $4,500, respectively, of net earnings applicable to these nine shopping centers. See Note B as to the Company's plan for its remaining Real Estate interests.

Store Closing

On July 12, 1978, the Board of Directors authorized the closing and demolition in 1982 of the existing downtown Detroit store facility for the Company's Hudson's department store operations, resulting in a provision for loss recorded in 1978 of $13,200. After related tax benefits, the net charge to earnings is approximately $7,500 or $.32 per share. The provision includes the write-off of land and buildings and anticipated demolition and lease acquisition costs. The Board of Directors also approved the plans to build a new downtown Detroit store facility, subject to various conditions including completion of a downtown shopping center project to include at least two other major department stores and receipt of funding from federal or local sources.

Unusual Expenses

Included in the caption Unusual Expenses in the Retail and Consolidated Results of Operations for 1978 are merger fees of $2,850 as a result of the Business Combination, the $13,200 provision for loss on Hudson's store closing, discussed above, and $3,700 of expenses provided for the disposal of certain retail operations, discussed in Note C. These unusual expenses decreased net income by approximately $.52 per share.

NOTE B. DISCONTINUED OPERATIONS OF REAL ESTATE SEGMENT

In February 1979, the Board of Directors approved a formal plan for the future sale or other disposition during 1979 of its remaining Real Estate interests, other than those directly employed or to be employed in its Retail operations. Among the assets and liabilities to be disposed of are the Company's interests in 14 remaining shopping centers, three of which are wholly owned and 11 owned by joint ventures in which the Company has 50% or less interest (see Note F).

Details of the results of operations for the Real Estate segment are presented separately to illustrate the significant contribution of real estate gains during 1978. Income taxes applicable to the components of discontinued operations are $80,026 and $2,485 in 1978 and 1977, respectively, on the gain from Real Estate property sales and $2,528 and $3,716, respectively, on earnings from other Real Estate operations.

Management has determined that an overall gain will result upon disposal of the Real Estate segment. Real Estate assets expected to be transferred to Retail or to be sold and liabilities anticipated to be assumed upon sale have been grouped separately in the Consolidated Statements of Financial Position.

NOTE C. PROVISION FOR LOSS ON DISPOSAL OF CERTAIN RETAIL OPERATIONS

In February 1979, the Board of Directors approved formal plans for the future sale or other disposition, in 1979, of Team Central Incorporated ("Team") and The Lipmans Division ("Lipmans"). The revenues and operating profit of these operations included in the Consolidated and Retail Results of Operations are:

	Team		Lipmans	
	1978	1977	1978	1977
Revenues	$38,592	$37,973	$49,387	$46,744
Operating profit (loss)	(759)	1,205	5,208	4,787

In connection with the Board approval, the Company established a provision for loss upon disposition of Team. This loss is included in the accompanying Consolidated and Retail Results of Operations in the caption Unusual Expenses (see Note A).

Subsequent to year end, the Company reached agreement in principle to dispose of Lipmans. A provision for loss upon sale was recognized in 1978 and has been included along with the loss provision of Team in the Consolidated and Retail Results of Operations (see Note A — Unusual Expenses).

NOTE D. ACCOUNTS RECEIVABLE AND CREDIT SALES

Deferred payment accounts receivable at February 3, 1979 include $425,171 of revolving charge accounts receivable, substantially all of which are due within one year, and $39,131 of revolving installment accounts, of which approximately 44% are due beyond one year.

The provision for bad debts on credit sales in 1978 and 1977 was $15,858 and $11,155, respectively. Finance charge revenues of $49,421 and $40,586 for 1978 and 1977, respectively, are included in net Retail revenues.

Credit sales were $1,196,150 and $1,023,300 in 1978 and 1977. Thirty day, revolving installment and revolving charge sales were approximately 82% of total credit sales in 1978 and 84% in 1977. Bank card sales made up the balance of credit sales.

NOTE E. INVENTORIES

Effective January 29, 1978 the Company changed its method of accounting for Mervyn's merchandise inventories from the lower of cost or market, as determined by the retail method applied on an average cost basis, to the retail method applied on a last-in, first-out (LIFO) basis. The Company believes the LIFO method will more fairly present the operating results of Mervyn's by reducing the effect of inflationary cost increases in inventory and thus match current costs with current revenues. The change had the effect of reducing merchandise inventories by $4,570 at February 3, 1979 and decreasing net earnings for the year then ended by $.10 per share. The change was made in the fourth quarter of 1978.

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Merchandise inventories detailed by segment are:

	Department	Low-Margin	Specialty	Mervyn's	Total
February 3, 1979..	$127,966	$132,133	$62,270	$71,068	$393,437
January 28, 1978..	121,280	107,476	52,373	56,218	337,347

The amounts of opening and closing inventories used in determining cost of sales are the total amounts above and $278,135 at January 29, 1977.

If the LIFO inventories had been valued by use of the first-in, first-out (FIFO) retail method, they would have been higher as follows:

	Department	Low-Margin	Specialty	Mervyn's	Total
February 3, 1979..	$35,594	$18,017	$12,461	$4,570	$70,642
January 28, 1978..	31,297	16,481	9,857	—	57,635

NOTE F. INVESTMENT IN JOINT VENTURES

The Real Estate line of business had partnership interests ranging from 24.5% to 50% in 16 joint ventures at February 3, 1979. Condensed combined financial statements of the joint ventures follow:

CONDENSED COMBINED RESULTS OF OPERATIONS FOR THE YEAR ENDED DECEMBER 31

	1978	1977
Operating Properties		
Rental revenue	$ 24,421	$ 16,440
Operating expenses	9,653	7,418
	14,768	9,022
Other (Income) Expense		
Interest expense (excluding interest capitalized of $481 in 1978 and $484 in 1977)	12,715	10,104
Depreciation and amortization	4,451	3,537
Development expense	856	961
Gain from property sales	(3,172)	(2,812)
Other, net	(285)	453
	14,565	12,243
Earnings (Loss)	$ 203	$ (3,221)

RECONCILIATION OF REAL ESTATE'S SHARE OF EARNINGS (LOSS) OF JOINT VENTURES

	1978	1977
Real Estate's share of operations (1)	$ (41)	$ (1,025)
Interest capitalized by joint venture	(160)	(161)
Other adjustments	(53)	146
Equity in loss as reflected in accompanying Real Estate results of operations	$ (254)	$ (1,040)

CONDENSED COMBINED STATEMENT OF FINANCIAL POSITION AT DECEMBER 31

ASSETS	1978	1977
Cash, receivables and other assets	$ 12,203	$ 14,933
Shopping centers and commercial property	106,555	99,751
Shopping centers under construction	24,129	6,923
Undeveloped land	32,599	30,831
	175,486	152,438
Less: Accumulated depreciation	(19,356)	(14,950)
	$156,130	$137,488
LIABILITIES		
Accounts payable and accrued expenses	$ 11,196	$ 14,284
Payable to Real Estate	10,332	6,746
Long-term debt (2)	142,435	121,099
Deferred gain on land sales	1,753	534
	165,716	142,663
PARTNERS' EQUITY		
Real Estate	(2,623)	(745)
Other partners	(6,963)	(4,430)
	(9,586)	(5,175)
	$156,130	$137,488

RECONCILIATION OF REAL ESTATE INVESTMENT IN AND ADVANCES TO JOINT VENTURES

	February 3, 1979	January 28, 1978
As shown above	$(2,623)	$ (745)
Advances to joint ventures	1,250	1,851
Cumulative effect of adjusting to Real Estate's accounting policies	24	61
Difference in basis of contributed property	(2,881)	(1,538)
As included in the caption Investments and Other Assets in accompanying Real Estate statements of financial position.	$(4,230)	$ (371)

(1) The tax benefit resulting from Real Estate's share of the loss is reflected in the provision for income taxes in the accompanying Real Estate Financial Statements.

(2) In certain situations, because of competitive market conditions and for favorable financial arrangements, the Real Estate subsidiaries have guaranteed repayment of joint venture debt until certain conditions have been met. Real Estate subsidiaries were contingently liable for $3.4 million of joint venture debt at February 3, 1979.

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NOTE G. LEASES

The Company owns the majority of its department and low-margin stores and equipment, and leases virtually all of its specialty and Mervyn's stores. Most of the lease agreements for department and Target stores are considered capital leases. All specialty store and the majority of Mervyn's store leases are considered operating leases. Additionally, Mervyn's leases equipment under agreements ranging to 10 years which are considered capital leases. The majority of the Company's leases require contingent rentals which are based upon a percentage of sales in excess of stipulated amounts. Additional payments for real estate taxes, insurance, and other expenses, where required, are included in occupancy costs in the accompanying results of operations. Most leases include options to renew with renewal terms varying from 5 to 25 years. Certain leases also include options to purchase the property.

The present value of the Company's minimum lease payments for all operating and capital leases having an initial or remaining noncancellable term in excess of one year at February 3, 1979, using incremental interest rates at the inception of the leases, is approximately $254,000.

Capitalizing certain of the Company's leases had the following effect on results of operations:

	1978	1977
Reduction in rent expense	$(10,299)	$(8,929)
Interest expense on capital leases	6,003	5,204
Depreciation expense on capital leases	6,020	5,221
Effect on:		
Earnings before income taxes	$ (1,724)	$(1,496)
Earnings per share	$ (.04)	$ (.03)

Including contingent rents on capital leases of $1,111 in 1978 and $979 in 1977, rent expense on leases with terms in excess of one year included in the results of operations was:

	1978	1977
Minimum rents	$27,701	$21,300
Contingent rents	9,047	8,803
Less: Sublease income	(1,038)	(1,118)
	$35,710	$28,985

Future minimum lease payments for capital leases used in determining the present value of the net minimum lease payments included in the Retail and Consolidated Statements of Financial Position and minimum lease payments for operating leases having initial or remaining noncancellable terms in excess of one year at February 3, 1979 are as follows:

	Capital Leases			Operating Leases (4)		
	Real Property	Equipment	Total	Real Property	Equipment	Total
1979	$ 5,168	$ 5,906	$ 11,074	$ 27,046	$ 2,649	$ 29,695
1980	5,725	5,775	11,500	26,477	1,744	28,221
1981	5,725	5,567	11,292	26,248	633	26,881
1982	5,654	4,720	10,374	25,521	550	26,071
1983	5,567	4,067	9,634	24,745	296	25,041
After 1983	86,629	10,250	96,879	226,348	—	226,348
Total (1)	114,468	36,285	150,753	$356,385	$ 5,872	$362,257
Estimated executory costs included	2,818		2,818			
Net minimum lease payments	111,650	36,285	147,935			
Interest included in total (2)	55,528	10,682	66,210			
Present value of net minimum lease payments (3)	$ 56,122	$25,603	$ 81,725			

(1) Minimum rental payments on capital leases have not been reduced by minimum sublease rentals of $1,556 due in the future under noncancellable subleases. Contingent rentals which are based on a percentage of sales in excess of stipulated amounts are not included in minimum rents.

Minimum payments for operating leases have not been reduced by minimum sublease rentals of $5,344 due in the future under noncancellable subleases.

(2) Interest necessary to reduce net minimum lease payments to present value.

(3) Reflected in the Retail and Consolidated Statements of Financial Position at February 3, 1979 as current and long-term capital lease obligations of $4,901 and $76,824, respectively.

(4) Includes $3,555 from Team and Lipmans (see Note C).

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Details of leased property under capital leases shown in the Retail and Consolidated Statements of Financial Position are:

	February 3, 1979	January 28, 1978
Real property	$68,122	$52,598
Equipment	33,435	30,716
Accumulated depreciation	(30,669)	(26,338)
	$70,888	$56,976

Real Estate, as lessor, leases space in regional shopping centers and commercial properties. All of these leases are operating leases. The Company has announced its intent to dispose of its investment in such centers in 1979 (see Note B). Consequently, future minimum rental revenue under noncancellable operating leases at February 3, 1979 has not been provided.

Included in the Real Estate Statement of Financial Position is property leased to others under operating leases of:

	February 3, 1979	January 28, 1978
Shopping Centers	$29,985	$148,463
Commercial Properties	7,323	7,613
Total	37,308	156,076
Less Accumulated Depreciation	1,939	63,557
	$35,369	$ 92,519

The Real Estate Results of Operations includes rental revenue from the above properties of:

	1978	1977
Rental Revenue:		
Minimum	$10,043	$20,989
Contingent	2,715	8,264
	$12,758	$29,253

NOTE H. LINES OF CREDIT

The Company had $81,500 in unsecured lines of credit with 15 banks at February 3, 1979, none of which was in use at year-end. Borrowings under the lines of credit are at the prime interest rate. As compensation for the line of credit arrangements, the Company was expected to and did maintain, during 1978, average net collected compensating balances (ledger balances less float, as computed by the banks) of $4,677 plus fees of $200 in lieu of balances. The balances were at all times legally subject to withdrawal without restriction, and served as part of the Company's operating cash balance.

During 1978 and 1977 average short-term borrowings (bank lines and commercial paper) were $1,167 and $13,600, and the maximum outstanding at the end of any month was $19,900 and $35,800, respectively. The weighted average interest rate was approximately 9.0% and 6.8%.

NOTE I. OUTSTANDING DRAFTS

Drafts outstanding of $51,367 at February 3, 1979 and $71,978 at January 28, 1978 are included in accounts payable in the Consolidated and Retail Statements of Financial Position.

NOTE J. LONG-TERM DEBT

A summary of long-term debt due beyond one year is as follows:

	February 3, 1979		January 28, 1978	
	Consolidated (Retail)	Discontinued Operations	Consolidated (Retail)	Discontinued Operations
Bank Term Loan	$ 9,375	$	$ 12,500	$
Sinking Fund Debentures	34,733		38,454	
Sinking Fund Notes	18,200		19,000	
Other Unsecured Notes — maturing at various dates to 1985 and bearing interest from 6% to 8%	2,862	200	3,018	
Mortgage Notes — notes and contracts for purchase of real estate, payable over periods ranging to 30 years from inception and bearing interest from 4¼% to 9½%	29,140	28,354	43,810	127,299
	$94,310	$28,554	$116,782	$127,299

The Bank Term Loan bears interest at a variable rate not to exceed an average of 7⅝% over the term of the loan agreement. The balance is payable in equal quarterly installments with final maturity on January 3, 1983. The Company is not required to maintain compensating balances.

The Sinking Fund Debentures bear interest at 7¾% ($18,750) and 9¾% ($15,983) and are redeemable through minimum annual sinking fund payments of $1,250 each to 1994 and 1995, respectively. The 5⅝% Sinking Fund Notes ($3,200) are payable $800 annually to 1982. The 8⅝% Sinking Fund Notes ($15,000) are part of a private placement agreement to borrow $50,000, the remaining $35,000 to be borrowed by November 15, 1979. Sinking fund payments begin in 1983 with final maturity in 1999.

The Bank Term Loan, the 7¾% and 9¾% Sinking Fund Debentures, and the 5⅝% and 8⅝% Sinking Fund Notes each contain varying provisions and restrictions for the protection of the lenders relating to working capital, sales of receivables, dividends and other restricted payments, and other restrictive covenants. Under the most restrictive of these provisions, $284,919 of retained earnings at February 3, 1979 was available for dividends and other restricted payments.

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The carrying value of land, buildings and equipment pledged as collateral to mortgage notes and contracts aggregated approximately $40,581 at February 3, 1979.

Aggregate annual principal payments on long-term debt for the next five years are: 1979 — $7,072, 1980 — $8,774, 1981 — $10,217, 1982 — $9,388, and 1983 — $5,191.

Included in the caption Interest Expense in Retail and Real Estate Results of Operations in 1978 and 1977 is interest of $418 and $1,363, respectively, on short-term funds advanced by Real Estate to Retail. Advances from Real Estate to Retail since the sale of the Company's shopping centers on May 18, 1978 are non-interest bearing and reflect the extent of the Company's investment of the proceeds of the sale in its Retail expansion program. Included in Real Estate Revenues for 1978 is $6,239 of interest income resulting from the short-term investment of a portion of the proceeds from the shopping center sale.

NOTE K. DEFERRED INCOME

Included in Deferred Income Taxes and Other Credits in the Real Estate Statement of Financial Position is deferred income of $7,849 and $4,612 at February 3, 1979 and January 28, 1978, respectively. The 1978 amount includes a $5,300 additional gain recorded based upon operations of the nine centers subsequent to their sale in May 1978. The Company will recognize the additional gain upon acceptance and payment by The Equitable Life Assurance Society during 1979 (see Note A).

NOTE L. COMMITMENTS AND CONTINGENCIES

Commitments for construction of new facilities and the purchase of real estate amounted to approximately $34,054 at February 3, 1979.

The Company and/or its subsidiaries are contingently liable for approximately $53,750 of mortgage debt at February 3, 1979 on certain office properties sold in 1976 and the shopping centers sold in 1978. The purchasers have agreed to indemnify the Company and/or its subsidiaries for any costs they might incur in relation to the mortgages.

The Company's 1972 through 1975 Federal income tax returns are currently under examination. No adjustments are anticipated which would have a material impact on earnings.

The nature and scope of the Company's business brings its properties, operations and representatives into regular contact with the general public and a variety of other business and governmental entities, all of which subject the Company to litigation arising out of the ordinary course of business. Considering the insurance which is in place for a portion of the litigation, and noting that the ultimate consequences of any particular litigation may not be presently conclusively determinable, it is the opinion of the management of the Company and of its legal counsel that none of the current litigation involving the Company or any of its subsidiaries or divisions will have a material effect on the operations or financial condition of the Company.

NOTE M. SHAREHOLDERS' INVESTMENT

	February 3, 1979	January 28, 1978
Preferred Stock, no par value, 200,000 shares authorized:		
$5/share cumulative, 24,886 and 25,675 shares outstanding	$ 249	$ 257
$6/share cumulative, 21,625 and 26,500 shares outstanding	216	265
	465	522
Common Stock, $1 par value, 60,000,000 shares authorized: 23,651,998 and 23,634,490 shares issued	23,652	23,634
Less Common Stock in treasury — none and 88,373 at par value	—	(88)
Additional paid-in capital	58,285	55,958
Retained earnings	725,963	499,781
	$808,365	$579,807

The Cumulative Convertible Preferred Stock is redeemable at $100 per share at February 3, 1979 ($5) and June 23, 1980 ($6) and convertible into 2⅔ shares of Common Stock per share. The liquidation value is $4,651 at February 3, 1979.

Beginning in the second quarter of 1978 the Company changed its method of accounting for dividends from recording the dividend as of shareholder record date to the earlier dividend declaration date. The change has been accounted for prospectively due to the immaterial impact on total shareholders' investment. The change resulted in five dividends (preferred and common) being recorded in 1978 including the dividend declared on January 10, 1979 of $9,549.

NOTE N. STOCK OPTIONS

The Company has five stock option plans for key employees, three of which apply only to Mervyn's. Under the 1969 and 1972 Employee Stock Option Plans, as amended, certain eligible employees were granted qualified and/or non-qualified stock options at 100% of market at dates of grant. Non-qualified stock options, incentive stock rights, and stock appreciation rights (SARS) have been granted to certain key employees at 100% of market at date of grant under two long-term Incentive Plans and a Tandem Option Plan, all adopted in 1976. The options issued under these plans are exercisable in cumulative annual installments of 25% of the optioned shares beginning 12 months after the grant date. The terms of the options vary between five and 10 years from the dates granted.

The 1972 Plan and the 1976 Tandem Option Plan also granted stock appreciation rights to option holders, permitting them to

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surrender exercisable non-qualified options in exchange for shares of the Company's stock having an aggregate market value, at the date of surrender, equal to the difference between the option price and the market value of the shares covered by the surrendered options. Because of a possible adverse impact on earnings resulting from the exercise of stock appreciation rights, the Company has encouraged appreciation rights holders to exercise options rather than the related stock appreciation rights. At February 3, 1979, outstanding non-qualified options for 258,621 shares had stock appreciation rights attached.

One of the Incentive Plans and the 1976 Tandem Option Plan also provide for the granting of performance shares (units) to certain key employees. Under the Tandem Option Plan, the pay out of performance units is in lieu of continuing the related and concurrently granted stock options and stock appreciation rights and is dependent upon the market price of the Company's stock. The units are payable in cash or stock at the Committee's discretion and all or a portion may be earned at the end of a four-year period beginning with the fiscal year in which the shares were granted. The number of performance shares awarded under the Incentive Plan is dependent upon the relative level of achievement of certain goals established at the beginning of the four-year performance period.

Awards of incentive stock rights under an Incentive Plan entitle the holder to receive, at the end of a four-year incentive period, shares of stock without payment to the Company, except for withholding taxes.

The Company's policy is to accrue compensation expense in anticipation of settlement of rights under the plans based on what mode of settlement the employee is most likely to elect in the case of SARS and the likelihood all or a portion of performance shares (units) will be earned at the end of the four-year grant period. Expense (income) of $667 and ($46) was charged (credited) to operations in 1978 and 1977, respectively, for the plans.

When options are exercised, the option price of the shares issued is credited to common stock and additional paid-in capital.

Shares reserved for future grant at February 3, 1979 and January 28, 1978 under all stock option plans were 221,996 and 631,977, respectively.

Shares under option were:

	1978		1977	
	Number of Shares	Price per Share	Number of Shares	Price per Share
Outstanding, beginning of year	436,038	$ 7.35 - $41.75	541,039	$ 7.35 - $28.50
Granted	180,362	33.91 - 43.19	88,283	21.10 - 41.75
Cancelled	(24,361)	7.94 - 37.25	(26,583)	7.94 - 34.81
Exercised	(92,505)	7.35 - 34.81	(166,701)	7.94 - 28.50
Outstanding, end of year	499,534	$ 7.35 - $43.19	436,038	$ 7.35 - $41.75
Performance shares (exclusive of those issued in conjunction with options) and incentive stock rights outstanding at end of year	56,203			
Total	555,737			
Shares reserved for future grants	221,996			
	777,733			
Number of shares exercisable	179,166			

NOTE O. GENERAL DESCRIPTION OF THE IMPACT OF INFLATION (UNAUDITED)

Inflation has been and will continue to be a factor impacting management's decisions. Although inflation has caused upward pressures on expenses and cost of sales, management has generally been able to offset such increases through operating efficiencies, sales productivity and price increases. Management believes these price increases are consistent with the voluntary price guidelines established through the Council on Wage and Price Stability.

Under the last-in, first-out (LIFO) inventory method followed by the Company the impact of inflation on cost of sales is effectively charged against current year net income.

While the cumulative impact of inflation over a number of years has resulted in higher estimated costs for the replacement of existing property and equipment, these increases have been partially offset by changes in design and construction of stores, improvements in fixturing, and technological advances in equipment which often increase productivity. Although management believes the replacement of certain existing assets with newer more efficient assets would reduce operating expenses, the savings cannot be quantified.

Dayton Hudson's annual report Form 10-K (a copy of which is available upon request) contains quantitative information with respect to estimated replacement cost of inventories and property and equipment at February 3, 1979 and January 28, 1978, and the estimated effect of such costs on cost of sales and depreciation expense for the years then ended.

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NOTE P. PENSION AND SAVINGS AND STOCK PURCHASE PLANS

Contributions to the Company's four defined benefit pension plans and supplemental retirement plan for 1978 and 1977 were $10,201 and $9,470, respectively. The plans' combined assets and liabilities were:

	December 31 1978	December 31 1977
ASSETS		
Insurance contracts	$ 11,463	$11,378
Fixed income securities	29,012	31,755
Equity securities	54,816	40,723
Total Assets at Cost (market value: 1978, $94,136; 1977, $84,866)	$ 95,291	$83,856
LIABILITIES AND EXCESS OF ASSETS OVER BENEFITS		
Vested benefits	$109,496	$95,642
Accrued benefits not vested	6,147	3,329
Unfunded liability of two plans	(22,006)	(16,436)
Excess of assets over benefits of two plans	1,654	1,321
Total Liabilities	$ 95,291	$83,856

Contributions to the Savings and Stock Purchase Plan by the Company in 1978 and 1977 were $2,718 and $2,380. The condensed assets, liabilities and equity of the plan were:

	December 31 1978	December 31 1977
ASSETS		
Investments at market value:		
Dayton Hudson Stock Fund	$11,281	$13,157
Fixed Income Fund	15,860	11,427
Equity Fund	28,008	23,751
Total Assets	$55,149	$48,335
LIABILITIES AND EQUITY		
Funds payable for securities and plan withdrawals	$ 1,049	$ 893
Plan equity	54,100	47,442
Total Liabilities and Equity	$55,149	$48,335

NOTE Q. INCOME TAX EXPENSE

The components of the provision for income taxes are:

	1978 Total	1978 Federal	1978 State	1977 Total	1977 Federal	1977 State
Consolidated (Retail):						
Current	$ 96,381	$79,003	$17,378	$82,492	$68,725	$13,767
Deferred	4,880	4,764	116	12,957	11,593	1,364
Total	$101,261	$83,767	$17,494	$95,449	$80,318	$15,131
Discontinued Operations:						
Current	$ 89,379	$77,883	$11,496	$ 7,288	$ 6,122	$ 1,166
Deferred	(6,825)	(6,470)	(355)	(1,087)	(844)	(243)
Total	$ 82,554	$71,413	$11,141	$ 6,201	$ 5,278	$ 923

Deferred income taxes are provided for income and expenses which are recognized in different accounting periods for financial reporting than for income tax purposes. A description of the timing differences and the related deferred taxes are as follows:

	1978 Consolidated (Retail)	1978 Discontinued Operations	1977 Consolidated (Retail)	1977 Discontinued Operations
Excess of tax over book (book over tax) depreciation	$ 1,556	$ (4,712)	$ 397	$ (1,215)
Deferred income on installment sales	12,072	(1,384)	15,044	(878)
Lease capitalization	(904)	—	(763)	—
Writedown and cost to demolish assets	(5,880)	(1,373)	(1,113)	335
Other	(1,964)	644	(608)	671
	$ 4,880	$ (6,825)	$12,957	$ (1,087)

Based on the Company's anticipated future operations and expenditures and current income tax policies, no substantial reduction in the deferred income tax balance is anticipated in the succeeding three years.

Report of Independent Auditors

Board of Directors and Shareholders
Dayton Hudson Corporation
Minneapolis, Minnesota

We have examined the statements of financial position of Dayton Hudson Corporation and subsidiaries and of their Retail and Real Estate Operations as of February 3, 1979 and January 28, 1978, and the related statements of results of operations, shareholders' investment and changes in financial position for the years then ended. We have also examined the Ten-Year Comparisons and the Segment Information included in the Five-Year Segment-of-Business Comparisons on pages 34-37. Our examinations were made in accordance with generally accepted auditing standards and, accordingly, included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances. We did not examine the financial statements of Mervyn's for any periods ended prior to February 3, 1979. The financial statements of Mervyn's for the year ended January 28, 1978, not shown separately herein, constitute approximately 10% of total assets at January 28, 1978 and approximately 15% of total revenues for the year then ended. Such financial statements were examined by other independent accountants, whose report dated March 3, 1978, expressed an unqualified opinion on those financial statements.

In our opinion, based on our examination and the report of such other independent accountants, the financial statements referred to above present fairly the financial position of Dayton Hudson Corporation and subsidiaries at February 3, 1979 and January 28, 1978, and the results of their operations and changes in their financial position for the years then ended, in conformity with generally accepted accounting principles applied on a consistent basis. It is also our opinion that the financial statements referred to above of the Corporation's Retail and Real Estate Operations are presented fairly in conformity with the accounting practices described in the Summary of Accounting Policies set forth in the financial statements, applied on a consistent basis. Further, it is our opinion, based on our examination and the report of such other accountants, that the Ten-Year Comparisons and the Segment Information included in the Five-Year Segment-of-Business Comparisons fairly present the information set forth therein.

Ernst & Ernst

Minneapolis, Minnesota
March 23, 1979

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NOTE H. QUARTERLY REVIEW (UNAUDITED)

The following is a summary of unaudited quarterly results of operations for 1978 and 1977:

(Millions of dollars, except per share data)

1978	Consolidated and Retail (4)					Discontinued Operations (Real Estate) (4)				
	First	Second	Third	Fourth	Total Year	First	Second	Third	Fourth	Total Year
Revenues										
As Reported	$567.0	$650.6	$703.7	$1,040.6	$2,961.9	$10.4	$ 5.4	$ 4.7	$ 5.1	$ 25.6
Gross Profit (1, 3)										
As Reported	$170.4	$186.6	$217.5	$ 332.0	$ 906.5	$ 6.6	$ 3.5	$ 3.3	$ 8.7	$ 22.1
Net Earnings										
As Reported	$ 11.6	$ 3.6	$ 23.0	$ 60.2	$ 98.4	$ .9	$152.6	$ 1.7	$12.1	$167.3
Adjustments for Start-up Costs and Leases (2)	(.4)	(.3)	(.4)	.3	(.8)	—	—	—	—	—
As Restated (Retail)	11.2	3.3	22.6	60.5	97.6					
Discontinued	.9	152.6	1.7	12.1	167.3	$ .9	$152.6	$ 1.7	$12.1	$167.3
As Restated (Consolidated)	$ 12.1	$155.9	$ 24.3	$ 72.6	$ 264.9					
Net Earnings Per Share										
As Reported	$ .49	$ .15	$ .97	$ 2.55	$ 4.16	$ .04	$ 6.47	$ .07	$ .51	$ 7.09
Adjustments for Start-up Costs and Leases (2)	(.02)	(.02)	(.01)	.01	(.04)	—	—	—	—	—
As Restated (Retail)	.47	.13	.96	2.56	4.12					
Discontinued	.04	6.47	.07	.51	7.09	$ .04	$ 6.47	$ .07	$ .51	$ 7.09
As Restated (Consolidated)	$ .51	$ 6.60	$ 1.03	$ 3.07	$ 11.21					

1977	Consolidated and Retail (4)					Discontinued Operations (Real Estate) (4)				
	First	Second	Third	Fourth	Total Year	First	Second	Third	Fourth	Total Year
Revenues (3)										
Dayton Hudson, As Reported	$418.0	$469.0	$519.7	$ 719.0	$2,125.7	$ 9.1	$ 10.0	$10.0	$14.5	$ 43.6
Mervyn's, As Reported	68.6	80.5	93.0	126.9	369.0	—	—	—	—	—
As Restated	$486.6	$549.5	$612.7	$ 845.9	$2,494.7	$ 9.1	$ 10.0	$10.0	$14.5	$ 43.6
Gross Profit (1, 3)										
Dayton Hudson, As Reported	$121.8	$132.9	$158.4	$ 223.7	$ 636.8	$ 5.2	$ 5.5	$ 6.0	$ 8.0	$ 24.7
Mervyn's, As Reported	23.0	26.6	32.5	44.3	126.4	—	—	—	—	—
As Restated	$144.8	$159.5	$190.9	$ 268.0	$ 763.2	$ 5.2	$ 5.5	$ 6.0	$ 8.0	$ 24.7
Net Earnings										
Dayton Hudson, As Reported	$ 7.8	$ 9.7	$ 17.7	$ 39.5	$ 74.7	$ .3	$ 1.7	$ .7	$ 3.5	$ 6.2
Mervyn's, As Reported	2.3	2.7	4.3	8.5	17.8	—	—	—	—	—
Adjustments for Start-up Costs and Leases (2)	(.3)	(.3)	(.2)	—	(.8)	—	—	—	—	—
As Restated (Retail)	9.8	12.1	21.8	48.0	91.7					
Discontinued	.3	1.7	.7	3.5	6.2	$ .3	$ 1.7	$ .7	$ 3.5	$ 6.2
As Restated (Consolidated)	$ 10.1	$ 13.8	$ 22.5	$ 51.5	$ 97.9					
Net Earnings Per Share										
Dayton Hudson, As Reported	$ .48	$ .61	$ 1.11	$ 2.46	$ 4.66	$ .02	$ .11	$ .04	$ .22	$ .39
Mervyn's, As Reported	.24	.29	.45	.90	1.88	—	—	—	—	—
Adjustments for Start-up Costs and Leases (2)	(.02)	(.01)	(.01)	.01	(.03)	—	—	—	—	—
As Restated (Retail)	.41	.52	.92	2.04	3.89					
Discontinued	.01	.07	.04	.15	.27	$ .01	$ .07	$ .04	$ .15	$ .27
As Restated (Consolidated)	$ .42	$ .59	$ .96	$ 2.19	$ 4.16					

(1) Consolidated and Retail — revenues less cost of sales, buying and occupancy. Discontinued Operations (Real Estate) — revenues less operating expenses.

(2) As explained in Note G, the Company retroactively implemented the provisions of FASB #13 on capitalization of leases in the fourth quarter of 1978. Prior quarters of 1978 and 1977 were restated accordingly.

Quarterly results were also restated to reflect Mervyn's adoption, in the fourth quarter of 1978, of the Company's policy for quarterly application of start-up costs (see Summary of Accounting Policies).

(3) Reclassifications were made to conform 1977 classifications with those of 1978. None of these changes had an effect on net earnings.

(4) Operating data for the first quarter of 1978 and for each quarter of 1977 were restated for the effect of Mervyn's pooling as discussed in Note A.

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Ten-Year Comparisons

Dayton Hudson Corporation and Subsidiaries

(Millions of dollars, except per share data)

The Ten-Year Comparisons should be read in conjunction with the Financial Review and Financial Statements.

(a) Earnings data for 1972 include extraordinary expense (as defined in 1972) of $0.7 million ($.04 per share).

(b) Dividends per common share are based on the historical number of average shares of the Corporation's Common Stock outstanding during the respective periods (see Note M).

(c) Consisted of 53 weeks.

REVENUES
Cost of retail sales, buying and occupancy
Interest expense
Depreciation and amortization
Interest and depreciation on capital leases
EARNINGS BEFORE INCOME TAXES
INCOME TAXES
NET EARNINGS (LOSS)
Continuing
Discontinued
Consolidated
PER COMMON SHARE
Net earnings
Continuing
Discontinued
Consolidated
Cash dividend[(b)]
Shareholders' investment
RETURN ON BEGINNING SHAREHOLDERS' INVESTMENT
CAPITAL EXPENDITURES
CONSOLIDATED YEAR-END FINANCIAL POSITION
Working capital
Property and equipment, net of depreciation
Leased property under capital leases, net of amortization
Non-current assets of discontinued segment
Long-term debt
Long-term capital lease obligations
Long-term liabilities of discontinued segment
Shareholders' investment
AVERAGE COMMON SHARES OUTSTANDING (Thousands)

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1978(c)	1977	1976	1975	1974	1973	1972(a,c)	1971	1970	1969
$2,961.9	2,494.7	2,125.8	1,852.2	1,609.3	1,461.7	1,325.2	1,135.7	984.0	892.8
$2,055.4	1,731.6	1,480.1	1,285.2	1,148.1	1,043.8	955.1	813.4	707.4	635.1
$ 8.2	9.9	8.9	9.0	14.7	13.5	13.2	12.7	12.4	8.5
$ 34.4	31.2	26.8	24.2	22.9	21.0	19.9	18.0	16.1	13.0
$ 12.0	10.4	8.7	7.8	6.7	5.2	4.5	2.8	2.5	2.2
$ 198.9	187.2	153.9	126.3	59.6	55.6	52.7	44.9	38.3	46.3
$ 101.3	95.5	79.4	65.6	29.6	27.5	26.2	21.0	19.9	23.8
$ 97.6	91.7	74.5	60.7	30.0	28.1	26.5	23.9	18.4	22.5
$ 167.3	6.2	2.5	(.1)	(.4)	2.1	2.9	2.0	1.5	1.8
$ 264.9	97.9	77.0	60.6	29.6	30.2	29.4	25.9	19.9	24.3
$ 4.12	3.89	3.18	2.63	1.31	1.24	1.17	1.08	.87	1.08
$ 7.09	.27	.11	—	(.01)	.09	.13	.09	.07	.09
$ 11.21	4.16	3.29	2.63	1.30	1.33	1.30	1.17	.94	1.17
$ 1.45	1.25	.96	.66	.585	.54	.52	.50	.50	.50
$ 33.98	24.40	21.12	18.51	16.58	15.70	14.78	13.96	13.79	13.06
45.7%	19.6	17.7	16 0	8.3	8.9	9.3	8.8	7.3	9.4
$ 156.1	104.9	76.1	33.4	48.7	40.0	43.7	31.5	44.5	62 0
$ 427.6	309.4	288.2	266.2	239.2	246.5	241.0	185.9	166.7	153.3
$ 472.2	379.7	317.2	280.0	274.3	260.6	249.3	244.4	235.0	206.9
$ 70.9	57.0	52.2	46.7	48.4	41.1	37.7	23.3	20.3	19.9
$ 48.2	150.0	136.7	146.4	145.7	133.9	117.4	116.1	118.5	110.2
$ 94.3	116.8	111.7	123 8	147.2	164.0	176.4	153.0	150.0	126.1
$ 76.8	62.0	56.6	50.6	51.5	43.9	40.0	25.2	21.8	21.2
$ 36.4	136.5	125.4	124.8	123.9	111.1	87.7	78 8	79.1	71.5
$ 808.4	579.8	499.2	435.9	378.6	358.5	339.7	316.1	293.5	272.7
23,597	23,500	23,325	22,947	22,469	22,466	22,428	21,839	20,826	20,620

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Five-Year Segment-of-Business Comparisons

Dayton Hudson Corporation and Subsidiaries

RETAIL SEGMENT INFORMATION

(Millions of Dollars)	1978 Dollar Amount	1978 Percent of Total	1977 Dollar Amount	1977 Percent of Total	1976 Dollar Amount	1976 Percent of Total
Revenues						
Department	$1,172 3	39.6%	$1,053.3	42.2%	$ 952.3	44.8%
Low margin	1,055.1	35.6	858.8	34.4	725.2	34.1
Specialty	255.0	8.6	213.6	8.6	180.3	8.5
Mervyn's	479.5	16.2	369.0	14.8	268.0	12.6
Total	$2,961.9	100.0%	$2,494.7	100 0%	$2,125.8	100.0%
Operating Profit (a)						
Department	$ 115 3	45 8%	$ 104.1	48.3%	$ 94.4	52 5%
Low margin	71.7	28.5	54.9	25.4	48 3	26.9
Specialty	20 2	8.0	19.1	8.9	12.8	7.1
Mervyn's (b)	44.5	17.7	37.4	17.4	24.2	13.5
Total	251.7	100.0%	215.5	100.0%	179.7	100.0%
Corporate expense	18.8		13.2		12.5	
Interest expense	8.2		9.9		8.9	
Interest expense on capital leases	6.0		5.2		4.4	
Earnings before unusual expenses and income taxes	218.7		187.2		153.9	
Unusual expenses (c)	19.8		—		—	
Earnings before income taxes	198.9		187.2		153.9	
Income taxes	101.3		95.5		79.4	
Net earnings from continuing operations	97.6		91.7		74.5	
Net earnings (loss) from discontinued operations	167.3		6.2		2.5	
Net earnings	$ 264.9		$ 97.9		$ 77.0	
Identifiable Assets at Year End						
Department	$ 683.6		$ 626.4		$ 543.7	
Low margin	412.4		327.6		265.0	
Specialty	104.7		85.1		70.8	
Mervyn's	218.4		155.2		116.6	
Corporate	66.2		51.6		70.2	
	1,485.3		1,245.9		1,066.3	
Real Estate (discontinued operations)	152.2		165.5		146.8	
Total	$1,637.5		$1,411.4		$1,213.1	
Depreciation and Amortization Expense						
Department	$ 20.7		$ 19.7		$ 17.7	
Low margin	11.0		9.7		8.1	
Specialty	3.4		2.9		2.5	
Mervyn's	4.9		3.8		2.6	
Corporate	.4		.3		.2	
	40.4		36.4		31.1	
Less amortization on capital leases	6.0		5.2		4.3	
Total	$ 34.4		$ 31.2		$ 26.8	
Capital Expenditures						
Department	$ 48.8		$ 43.4		$ 38.9	
Low margin	63.7		43.6		23.7	
Specialty	9.0		5.1		4.8	
Mervyn's	34.5		10.5		8.7	
Corporate	.1		2.3		—	
	156.1		104.9		76.1	
Less expenditures on capital leases	20.0		10.0		9.8	
Total	$ 136.1		$ 94.9		$ 66 3	
OTHER INFORMATION						
Operating Profit as a Percent of Revenues						
Department	9.8%		9 9%		9.9%	
Low margin	6.8		6.4		6.7	
Specialty	7.9		8.9		7.1	
Mervyn's (b)	9.3		10.1		9.0	
Number of Stores						
Department	51		46		44	
Low margin	73		64		56	
Specialty	413		364		313	
Mervyn's	51		42		35	
Retail Square Feet (Thousands)						
Department	10,799		10,126		9,690	
Low margin	7,909		6,999		6,185	
Specialty	1,548		1,346		1,182	
Mervyn's	3,902		3,154		2,566	
Start-up Costs (Millions)						
Department	$ 7.8		$ 6.7		$ 6.7	
Low margin	6.3		5.5		3.3	
Specialty	2.7		1.2		1.1	
Mervyn's	2.2		1.1		1.4	
Total	$ 19.0		$ 14.5		$ 12.5	

(a) Operating profit includes all revenue and expense items other than corporate expense, interest expense, unusual expenses, equity in losses and interest income from joint ventures, and income taxes.

(b) Mervyn's 1978 operating profit includes a $4.6 million charge for adoption of LIFO (see Note E of Notes to Financial Statements).

(c) Unusual expenses in 1978 include merger fees as a result of the business combination with Mervyn's, a provision for loss on the closing of Hudson's downtown store facility and costs provided for the disposal of certain retail operations.

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1975 Dollar Amount	1975 Percent of Total	1974 Dollar Amount	1974 Percent of Total
$ 888.7	48.0%	$ 823.3	51.2%
616.2	33.3	524.6	32.6
149.3	8.0	124.3	7.7
198.0	10.7	137.1	8.5
$1,852.2	100.0%	$1,609.3	100.0%
$ 83.2	54.0%	$ 52.4	62.5%
39.9	25.9	18.4	21.9
9.8	6.4	2.8	3.3
21.1	13.7	10.3	12.3
154.0	100.0%	83.9	100.0%
14.6		6.0	
9.0		14.7	
4.1		3.6	
126.3		59 6	
—		—	
126.3		59.6	
65.6		29.6	
60.7		30.0	
(.1)		(.4)	
$ 60.6		$ 29.6	
$ 489.7		$ 452.2	
232.1		214.8	
62.0		53.3	
82.1		60.4	
54.0		17.1	
919.9		797.8	
163.3		157.1	
$1,083.2		$ 954.9	
$ 16.1		$ 15.4	
7.5		7.4	
2.1		1.7	
2.0		1.3	
.2		.2	
27.9		26.0	
3.7		3.1	
$ 24.2		$ 22.9	
$ 19.2		$ 31.6	
6.3		5.0	
4.7		4.5	
3.1		7.4	
.1		.2	
33.4		48.7	
2.0		10 7	
$ 31.4		$ 38.0	
9.4%		6.4%	
6.5		3.5	
6.6		2.3	
10.7		7.5	
41		39	
52		50	
273		231	
26		24	
9,210		9,027	
5,865		5,542	
1,047		968	
1,855		1,676	
$ 2.8		$ 6.1	
1.3		.7	
1.0		1.1	
.3		.8	
$ 5.4		$ 8.7	

REAL ESTATE SEGMENT INFORMATION

(Discontinued Operations)

(Millions of Dollars)	1978	1977	1976	1975	1974
Revenues					
Total rental and other operating revenue	$ 23.8	$ 52.7	$ 49.1	$ 43.9	$ 34.2
Interest income	6.2	—	—	—	—
	30.0	52.7	49.1	43.9	34.2
Intersegment revenue (eliminated in consolidation)	4.4	9.1	8.3	7.6	6.0
Revenue from unaffiliated sources	25.6	43.6	40.8	36.3	28.2
Expenses and Other Income					
Operating expenses	8.7	18.9	18.7	16.1	13.9
Interest expense:					
Operating	3.6	8.1	8.5	8.8	7.1
Development	1.1	.2	.3	.4	1.6
Other	.2	.3	.5	.3	.5
Total interest	4.9	8.6	9.3	9.5	9.2
Depreciation and amortization	2.3	5.7	6.5	6.1	4.9
Development expense	2.9	1.5	1.9	2.0	1.4
Gain from property sales	(2.0)	(5.0)	(3.3)	(.9)	(2.3)
Other, net	1.2	.8	.7	2.2	1.4
Equity in loss of joint ventures	.3	1.0	2.9	2.4	1.1
Interest income from advances to joint ventures	(.7)	(.3)	(.5)	(.9)	(.4)
	17.6	31.2	36.2	36.5	29.2
Gain from sale of shopping centers	241.8	—	—	—	—
Earnings (Loss) Before Income Taxes	249.8	12.4	4.6	(.2)	(1.0)
Income Taxes	82.5	6.2	2.1	(.1)	(.6)
Net Earnings (Loss)	$167.3	$ 6.2	$ 2.5	$ (.1)	$ (.4)
Operating Profit (a)	$254.6	$ 22.2	$ 16.8	$ 11.2	$ 9.3
Corporate Expense (included above)	$ .3	$ .5	$ .5	$ .4	$ .4
Assets at Year End					
Identifiable assets	$156.4	$165.9	$145.7	$162.8	$154.1
Investments in/advances to joint ventures	(4.2)	(.4)	1.1	.5	3.0
Total	$152.2	$165.5	$146.8	$163 3	$157.1
Capital Expenditures	$ 9.8	$ 27.0	$ 16.8	$ 9 6	$ 22 9

Dayton Hudson Corporation operates a Retail business which is divided into four segments — department, low-margin, specialty and Mervyn's See pages 4-10 for discussion.

Retail revenues are principally from unaffiliated customers. Intersegment revenues are immaterial.

Real Estate revenues include rental income from unaffiliated tenants, as reported in the Real Estate (discontinued operations) Results of Operations, and intersegment revenues with the department and specialty segments Intersegment revenues are at similar rates and are accounted for on the same basis as revenues from unaffiliated tenants.

Identifiable assets by industry segment are those assets that are used in the operations of each segment. The Summary of Accounting Policies beginning on page 23 contains a more specific description of the methods used to allocate assets between the Retail and Real Estate lines of business. Corporate assets consist primarily of cash and short-term investments.

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At the close of 1978, Dayton Hudson Corporation was operating 588 stores in 44 states.

Department Stores

■ Hudson's ■ Dayton's ■ Diamonds
■ Lipmans ■ John A. Brown

At year-end, the department store group consisted of five operating companies: *Hudson's* in Michigan and Ohio; *Dayton's* in Minnesota, North Dakota and South Dakota; *Diamonds* in Arizona and Nevada; *Lipmans* in Oregon; and *John A. Brown* in Oklahoma.

Low-Margin Stores

■ Target ■ Lechmere

The low-margin group consists of *Target,* a low-margin department store chain operating in 10 midwestern and southwestern states, and *Lechmere,* a New England hardlines retailer with particular strength in major appliances. Both operate high-volume, low-expense stores featuring dominant selections of national-brand merchandise.

Specialty Stores

■ B. Dalton Bookseller
■ Dayton Hudson Jewelers
■ Team Electronics

The specialty store group consists of three multi-store companies: *B. Dalton Bookseller,* a national bookstore chain; *Dayton Hudson Jewelers,* a group of six regional fine-jewelry retailers, and *Team Electronics,* a chain of consumer-electronics stores.

Mervyn's

Mervyn's is a softlines retail company with 51 stores in California, Nevada, Arizona and New Mexico. Mervyn's stores feature a popularly priced balance of nationally branded and private label apparel, accessories and household softgoods.

DEPARTMENT STORES	No. of Stores	Retail Sq. Ft.* (000)
Hudson's		
Detroit, Mich.	9	4,306
Pontiac, Mich.	1	289
Flint, Mich.	1	268
Toledo, Ohio	1	187
Ann Arbor, Mich.	1	187
Grand Rapids, Mich.	1	122
Saginaw, Mich.	1	122
	15	5,481
Dayton's		
Minneapolis-St. Paul, Minn.		
Department Stores	7	2,297
Home Stores	3	178
Rochester, Minn.	1	155
St. Cloud, Minn.	1	102
Fargo, N.D.	1	115
Grand Forks, N.D.	1	100
Sioux Falls, S.D.	1	100
	15	3,047
Diamonds		
Phoenix, Ariz.	6	848
Tucson, Ariz.	1	98
Las Vegas, Nev.	2	166
	9	1,112

Department Stores

Low-Margin Stores

Specialty Stores

Mervyn's

*Retail square feet is total square feet less office, warehouse and vacant space.
**Discontinued as of March 30, 1979.

Dayton Hudson Corporation

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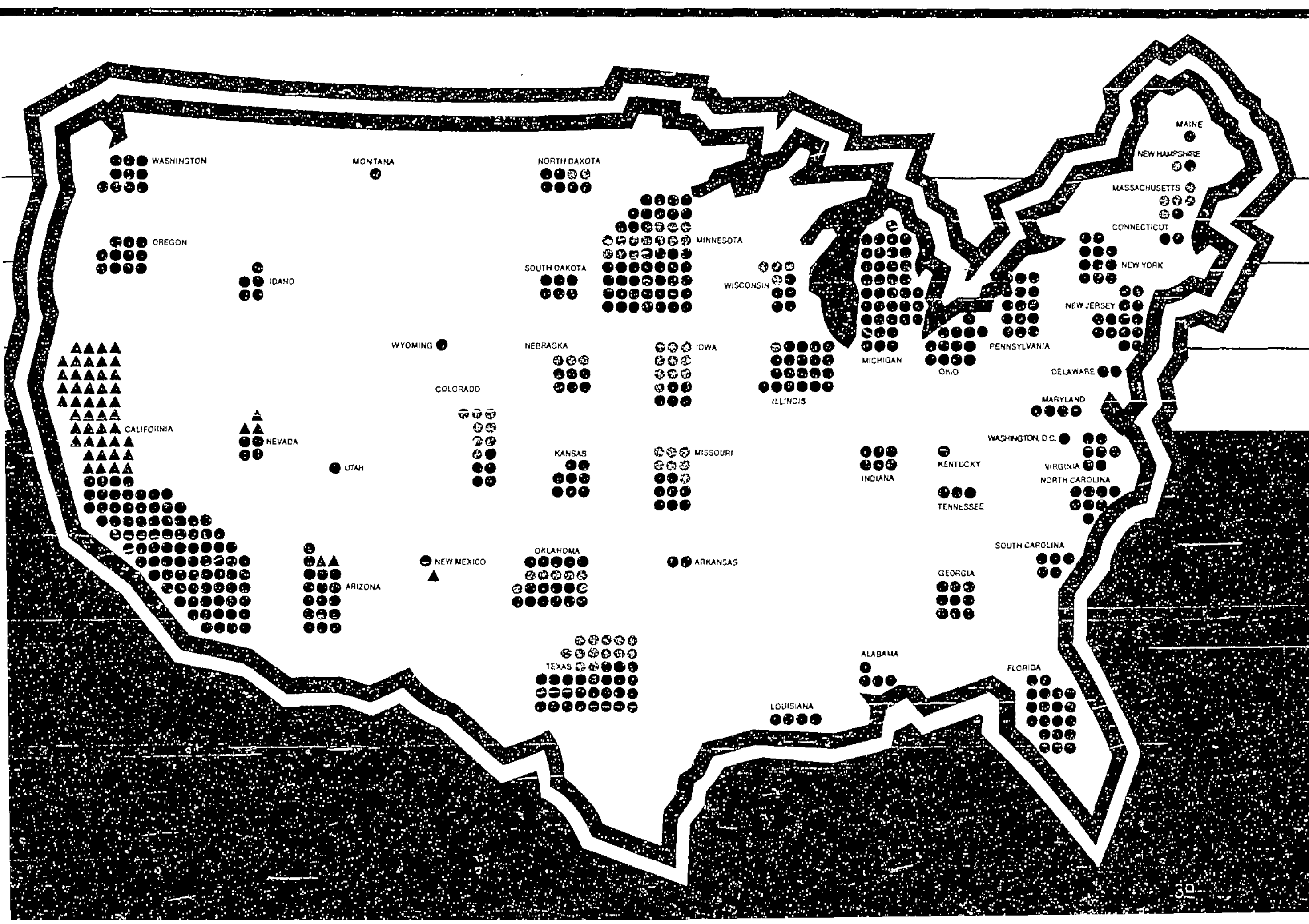
Lipmans**		
Portland, Ore.	4	499
Salem, Ore.	1	75
Corvallis, Ore.	1	47
Eugene, Ore.	1	50
	7	671
John A. Brown		
Oklahoma City, Okla.	3	287
Tulsa, Okla.	2	201
	5	488
Total Department Stores	51	10,799

LOW-MARGIN STORES	No. of Stores	Retail Sq. Ft.* (000)
Target		
Minneapolis-St. Paul, Minn.	12	1,298
Duluth, Minn.	1	96
Dallas-Ft. Worth, Texas	6	704
Houston, Texas	7	785
St. Louis, Mo.	7	790
Denver, Colo.	7	714
Colorado Springs, Colo.	1	130
Oklahoma City, Okla.	4	391
Tulsa, Okla.	2	226
Milwaukee, Wis.	4	452
Omaha, Neb.	3	310
Des Moines, Iowa	3	315
Ames, Iowa	1	45
Bettendorf, Iowa	1	80
Cedar Rapids, Iowa	1	80
Clinton, Iowa	1	60
Fort Dodge, Iowa	1	61
Mason City, Iowa	1	50
Ottumwa, Iowa	1	50
Moline, Ill.	1	80
Grand Forks, N.D.	1	100
Fargo, N.D.	1	100
	67	6,917
Lechmere		
Boston, Mass.	4	751
Springfield, Mass.	1	159
Manchester, N.H.	1	82
	6	992
Total Low-Margin Stores	73	7,909

SPECIALTY STORES	No. of Stores	Retail Sq. Ft.* (000)
Dayton Hudson Jewelers		
J. E. Caldwell		
Philadelphia, Pa.	3	21
Harrisburg, Pa.	1	5
Moorestown, N.J.	1	4
Wilmington, Del.	1	2
Newark, Del.	1	2
	7	34
J. B. Hudson		
Minneapolis-St. Paul, Minn.	7	27
Rochester, Minn.	1	2
Omaha, Neb.	1	5
	9	34
J. Jessop & Sons		
San Diego, Calif.	7	27
C. D. Peacock		
Chicago, Ill.	7	37
Shreve's		
San Francisco, Calif.	7	28
C. W. Warren		
Detroit, Mich.	8	21
Total Jewelry Stores	45	181



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B. Dalton Bookseller	No. of Stores	Retail Sq. Ft.* (000)
Northeast	45	216
Southeast	59	194
Midwest	98	331
South Central	50	178
Northwest	20	61
Southwest	85	358
	357	1,338
Team Electronics		
Colorado	1	2
Illinois	1	3
Kansas	4	12
Minnesota	1	3
Oklahoma	4	9
	11	29
Total Specialty Stores	413	1,548

MERVYN'S	No. of Stores	Retail Sq. Ft.* (000)
San Francisco Bay Area, Calif.	14	1,045
Los Angeles, Calif.	9	706
San Jose, Calif.	6	499
Sacramento, Calif.	3	202
San Diego, Calif.	2	163
Reno-Sparks, Nev.	2	127
Phoenix, Ariz.	2	192
Modesto, Calif.	1	62
Merced, Calif.	1	60
Visalia, Calif.	1	60
Salinas, Calif.	1	60
Chico, Calif.	1	60
Santa Rosa, Calif.	1	53
Bakersfield, Calif.	1	100
Fresno, Calif.	1	105
Stockton, Calif.	1	81
Marysville, Calif.	1	66
Capitola, Calif.	1	75
Las Vegas, Nev.	1	80
Albuquerque, N.M.	1	106
Total Mervyn's Stores	51	3,902
Total Retail	588	24,158

*Retail square feet is total square feet less office, warehouse and vacant space.

DEPARTMENT STORES

Hudson's

Chairman and Chief Executive Officer
Joseph L. Hudson, Jr.

President
Theodore A. Bintz

Dayton's

President and Chief Executive Officer
P. Gerald Mills

Diamonds

Chairman and Chief Executive Officer
Arthur F. (Jim) Baumann

President
Harvey L. Lowenthal

John A. Brown

President and Chief Executive Officer
James W. Sherburne, Jr.

LOW-MARGIN STORES

Target

Chairman and Chief Executive Officer
Kenneth A. Macke

President
Bruce G. Allbright

Lechmere

President and Chief Executive Officer
David Banker

SPECIALTY STORES

B. Dalton Bookseller

President and Chief Executive Officer
Floyd Hall

Dayton Hudson Jewelers

President and Chief Executive Officer
Sherman A. Swenson

Team Electronics

President and Chief Executive Officer
Paul D. Hagstrum

MERVYN'S

Chairman and Chief Executive Officer
Mervin G. Morris

President
John F. Kilmartin

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Dayton-Hudson Corporation

DIRECTORS

William A. Andres, Chairman of the Board[b]

Bruce B. Dayton, Chairman, Finance Committee[b]

K. N. Dayton, Chairman, Executive Committee[b]

***Donald J. Hall,** President and Chief Executive Officer, Hallmark Cards, Inc. (greeting card manufacturer)[a][b]

Joseph L. Hudson, Jr., Chairman of Hudson's

Stephen F. Keating, Vice Chairman of the Board, Honeywell Inc. (automation equipment manufacturer)[a][b]

Howard H. Kehrl, Executive Vice President, General Motors Corporation (manufacturer of transportation equipment)[b]

Bruce K. MacLaury, President, The Brookings Institution (research and planning organization)[b]

David T. McLaughlin, President, The Toro Company (yard care equipment manufacturer)[a][b]

****Mervin G. Morris,** Chairman of Mervyn's

Stephen L. Pistner, President

Richard L. Schall, Vice Chairman

William H. Spoor, Chairman of the Board, The Pillsbury Company (diversified food producer)[a][b]

Paul N. Ylvisaker, Dean of the Graduate School of Education, Harvard University[b]

Shirley Young, Executive Vice President, Grey Advertising, Inc. (advertising agency)[a][b]

(a) Audit Committee
(b) Executive Committee

* Elected September 1978
** Elected January 1979

OFFICERS

William A. Andres, Chairman and Chief Executive Officer

Stephen L. Pistner, President and Chief Operating Officer

Richard L. Schall, Vice Chairman and Chief Administrative Officer

K. N. Dayton, Chairman, Executive Committee

Gerald R. Gallagher, Senior Vice President

Joseph L. Hudson, Jr., Senior Vice President

Kenneth A. Macke, Senior Vice President

P. Gerald Mills, Senior Vice President

Mervin G. Morris, Senior Vice President

Albert B. Perlin, Senior Vice President and Secretary

C. George Scala, Senior Vice President

Wayne E. Thompson, Senior Vice President

Gerald R. Dirks, Vice President

David W. Haskin, Vice President

Allan L. Pennington, Vice President

Willard C. Shull III, Vice President-Finance

Karol D. Emmerich, Treasurer

Peter Corcoran, Assistant Treasurer

William E. Harder, Assistant Secretary

William P. Hise, Assistant Secretary

TRANSFER AGENTS AND REGISTRARS

Northwestern National Bank of Minneapolis

The Northwestern Trust Company, New York City

10-K REPORT

A copy of the Form 10-K annual report filed with the Securities and Exchange Commission for Dayton Hudson's fiscal year ended February 3, 1979, is available at no charge to shareholders on request. Write to: Director, Financial Relations.

SHAREHOLDER INVESTMENT SERVICE

The Shareholder Investment Service is a cost-free way for Dayton Hudson Corporation shareholders to acquire additional shares of the Corporation's common stock through automatic dividend reinvestment and voluntary cash purchase. All holders of Dayton Hudson common stock may participate. For more information, write Director, Financial Relations.

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